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No. 1023
In the Supreme Court of the United States

WELLS FARGO BANK and A. B. NEIL, JR.,
as Executors of the Will
of Louis L. Pendleton, Deceased.

Petitioners,

vs.

HOWARD C. PLATT, ROBERT C. PLATT, a minor,
and MARILYN A. PLATT, a minor,
by his and her Guardian Ad Litem,
Howard C. Platt,

Respondents.

Petition for Writ of Certiorari to the District Court of Appeal of the State of California First Appellate District

EDWIN S. PILLSBURY
155 Montgomery Street
San Francisco 4, California
Attorney for Petitioners

DAVID C. DUNLAP
PILLSBURY & DUNLAP
155 Montgomery Street
San Francisco 4, California

PAUL I. MYERS, JR.
681 Market Street
San Francisco 5, California
Of Counsel

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Petition for Writ of Certiorari to the District Court of Appeal of the State of California First Appellate District

Petitioners, WELLS FARGO BANK and A. B. NEIL, JR., as executors of the will of Louis L. Pendleton, Deceased, pray that a Writ of Certiorari issue to review a Judgment of the District Court of Appeal of the State of California, First Appellate District, Division Two, entered on November 27, 1963. This Judgment affirmed a Judgment of the Superior Court of the State of California in and for the County of San Mateo which had ordered enforcement of a

trust notwithstanding Petitioners' defense that the trust was for a purpose which was illegal under Federal law.

OPINIONS BELOW

The Opinion of the California District Court of Appeal was dated November 27, 1963 (App. 1-15).* It has not yet been officially reported. It is reported unofficially in 222 Adv. Cal. App. 718 and 35 Cal. Reptr. 377. An Opinion dated May 10, 1961 (App. 18-68) was also rendered by the California Superior Court which was the trial court. This Opinion is unreported.

JURISDICTION

Under California practice the Judgment of the District Court of Appeal is comprised in the last paragraph of its opinion. (App. 15) The judgment was dated and entered November 27, 1963. On December 17, 1963 the District Court of Appeal made an Order denying Petitioners' petition for a rehearing (App. 16); and on January 22, 1964, the Supreme Court of the State of California made its Order denying Petitioners' Petition for a Hearing by that court. (App. 17.)

The jurisdiction of this court is invoked under 28 U.S.C. § 1257(3).

QUESTIONS PRESENTED

1. Do the principles which preclude court enforcement of illegal transactions apply to transactions entered into for the purpose of accomplishing an unlawful evasion of taxes under the Internal Revenue Code? If so, will enforcement or nonenforcement of a patently evasive transac-

*In view of the total length of the two opinions below to be printed, the Appendix material is presented under separate binding.

tion depend on the subjective good or bad faith of the parties?

2. Should court enforcement be granted for a constructive trust which was created for the purpose of enabling the parties to make a false claim to the benefit of the marital deduction in the determination of Federal Estate Taxes?

3. Under the Federal Estate Tax law, is the marital deduction allowable for property given by will, apparently outright, to a surviving spouse where the testator executed the will in reliance upon oral and written agreements of the surviving spouse that the spouse would hold a life estate only and that the property would thereafter go to third parties designated by the testator?

STATUTES AND REGULATIONS INVOLVED

Section 812 of the Internal Revenue Code of 1939 (as amended by the Revenue Act of April 2, 1948, ch. 168, § 361(a), 62 Stat. 117), 26 U.S.C. 812 (1952 Ed.)* provided in relevant part as follows:

"§ 812. *Net estate.*

For the purpose of the tax the value of the net estate shall be determined, in the case of a citizen or resident of the United States by deducting from the value of the gross estate—"

* * * * * * *

"*(e) Bequests, etc., to surviving spouse.*

(1) Allowance of marital deduction.

(A) In general. An amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

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*The counterpart of the quoted provisions under the 1954 Internal Revenue Code is 26 U.S.C. 2056(a), (b)(1)(A)-(B).

(B) Life estate or other terminable interest. Where, upon the lapse of time, upon the occurrence of an event or contingency, or upon the failure of an event or contingency to occur, such interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed with respect to such interest—

(i) if an interest in such property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and

(ii) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse;"

Estate Tax Regulations, 26 C.F.R. § 81.47b(d) (1949 Ed., pocket supp.)*, added by Treasury Decision 5699 of May 19, 1949, 14 F.R. 2633, provided in relevant part as follows:

"(d) *Interest in property which another person may possess or enjoy.* (1) Section 812 (e) (1) (B) provides that no marital deduction shall be allowed with respect to certain property interests (referred to generally as 'terminable interests') which passed from the decedent to his surviving spouse, in case:

(i) An interest in the same property passed at any time (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such spouse (or the estate of such spouse), and

(ii) By reason thereof, such person (or his heirs or assigns) may possess or enjoy any part of such prop-

*Counterpart of this provision appears in the present regulations in 26 C.F.R. § 20.2056(b)-1.

erty after the termination or failure of the interest therein which passed from the decedent to his surviving spouse.

(2) The foregoing provision is applicable only where interests in the same property passed from the decedent both to his surviving spouse, and to some other person (for less than an adequate and full consideration in money or money's worth), and is applicable irrespective of whether both such interests passed from the decedent at the same time or under the same instrument. Under such circumstances, if the other person to whom an interest passed may, by reason thereof, possess or enjoy any part of the property after the termination or failure of the interest therein which passed from the decedent to his surviving spouse, the latter interest is a 'nondeductible interest'."

Estate Tax Regulations, 26 C.F.R. § 81.47a(b)(2)(ii) (1949 Ed., pocket supp.)*, added by Treasury Decision 5699 of May 19, 1949, 14 F.R. 2629, provided in relevant part as follows:

"The deduction may not be taken with respect to a property interest which passed to such spouse merely as trustee, or subject to a binding agreement by such spouse to dispose of such interest in favor of a third person."

STATEMENT OF THE CASE

In 1948, by amendment of the Internal Revenue Code, Congress provided for the marital deduction in the determination of a decedent's taxable estate for Federal Estate Tax purposes. The deduction can be taken for property up to one-half of the "gross estate" bequeathed by a decedent to his surviving spouse. The deduction is expressly

*Substantially the same provision appears in the present regulations in 26 C.F.R. § 20.2056(e)-2(a).

limited, however, to property which passed to the surviving spouse outright and with no other person designated by the decedent to take the property upon the death of the spouse or other contingency. The deduction is not permitted for "terminable interests" (Int. Rev. Code 1939 § 812(e)(1)(B), quoted *supra* p. 4 and 1954 Code § 2056 (b)(1)). Thus, if the decedent has limited his surviving spouse to a life estate, the marital deduction is not available.

In the present case, the decedent, Gladys Pendleton, who was making a new will in October 1949, desired to limit her spouse, Col. Pendleton, to a life estate with the remainder interest to go to her nephew, Howard Platt, and his family. (Opinion on Appeal, App. 1-3; Findings, Cl. Tr. 356-7; R. Tr. 25.)* She also wanted her estate to have the benefit of the marital deduction. (R. Tr. 273, 281, 1146; see Opinion on Appeal, App. 2.) In order to accomplish this dual objective, the decedent, her husband, and her nephew entered into the following arrangement:

The decedent made a will in which one-half of the residue of her estate was left to her husband, apparently outright and without restriction; and the other one-half of the residue was bequeathed to the decedent's nephew, Howard Platt (Opinion on Appeal, App. 1). Prior to making the will, however, the decedent had received promises from her husband and her nephew that upon distribution of the residue of her estate to them, they would place the same in an irrevocable trust in which her husband would be limited to a life estate in a portion of the property and in which the property, upon her husband's death, would go to Howard Platt and members of his family. (Findings, Cl. Tr. 358.) Col. Pendleton and Howard Platt further

*"Cl. Tr." refers to Clerk's Transcript, and "R. Tr." refers to Reporter's Transcript of proceedings in the trial court.
"Findings" refers to Findings of Fact made by the trial court.

agreed with Mrs. Pendleton that they would sign a written agreement to this effect (Findings, Cl. Tr. 358). The written agreement* was read to and approved by Mrs. Pendleton prior to her execution of the will and was in fact signed on the same day. (Findings, Cl. Tr. 359; R. Tr. 64, 84, 333.) Mrs. Pendleton made her will in reliance upon these arrangements by which her husband was to be limited to a life estate and upon his death the property would go to the others whom she designated (Findings, Cl. Tr. 358, 398, 403).

In previous wills Mrs. Pendleton had provided for her husband's life estate by a testamentary trust (Findings, Cl. Tr. 354-355). The purpose of the changed arrangements was to secure the benefits of the marital deduction. (See Opinion of District Court of Appeal quoted *infra*, p. 10; R. Tr. 267-8, 276, 287, 1222-4.) This would be accomplished on the basis of the outright bequest to Col. Pendleton in Mrs. Pendleton's will, and Col. Pendleton would still be limited through the secret† trust to a life estate. This purpose was in fact carried out. Mrs. Pendleton died in 1950, and Howard Platt and Col. Pendleton, as co-executors of her estate, executed and filed a Federal Estate Tax Return in which the marital deduction was claimed on the basis of the outright bequest of one-half of the residue of the estate to Col. Pendleton without disclosure of the secret trust which would limit Col. Pendleton to a non-qualifying

*The terms of the written agreement are summarized in the Opinion on Appeal (App. 2-3). The agreement is set forth at length in the Opinion of the trial court. (App. 26-27).

†Constructive trusts of the type herein involved are recognized in California and have been referred to as "secret" trusts. *Gagner v. Purcell* (1916) 173 Cal. 495, 499, 160 Pac. 682, 684; *In re Sharp* (1911) 17 Cal. App. 634, 636, 120 Pac. 1079, 1080; *Prior v. Andrews* (1927) 83 Cal. App. 782, 791, 257 Pac. 560, 564.

life estate (Findings, Cl. Tr. 395). The question in the Federal Estate Tax Return schedule as to whether any person other than the surviving spouse claimed or contemplated claiming any interest in the property listed as passing to the surviving spouse was answered, "No". (Opinion on Appeal, App. 4.) As a result, some $36,000 in Federal Estate Taxes were evaded (R. Tr. 790-91).

The parties had had the advice of an attorney in planning and carrying out the foregoing arrangements. Counsel had advised that the marital deduction would not be allowable if Col. Pendleton were limited to a life estate by a testamentary trust (R. Tr. 1147) but that if Mrs. Pendleton made an outright bequest in her will, then her husband and her nephew could make any agreement between themselves which they desired, so long as no restrictions on the outright bequest "emanated" from Mrs. Pendleton (Opinion on Appeal, App. 2). Later on counsel prepared the Federal Estate Tax Return which the parties executed and filed. (Findings, Cl. Tr. 395.) Although the scheme which the parties adopted was so obviously evasive that Howard Platt himself referred to it as "shenanigans" (R. Tr. 63), the trial court found that the parties did what they did in good faith in reliance upon counsel's advice and without deliberate intent to violate the Federal law (Findings, Cl. Tr. 393, 395).

The trust was never fully activated, and in 1959 Howard Platt and his two children, Robert and Marilyn Platt, Respondents herein, filed this action to enforce the trust in the Superior Court in San Mateo County, California. (App. 5; Cl. Tr. 1.)

Col. Pendleton died prior to the trial of the case, and his executors, Petitioners herein, were substituted for him in the litigation (App. 6).

Raising and Disposition of Federal Questions in Courts Below.

The federal question as to the consequences of the illegality of the purpose of the transaction under the Federal Estate Tax law has been the primary issue throughout the case. It was first raised in Col. Pendleton's first adversary appearance by demurrer filed January 13, 1960. In the demurrer defendant specifically asserted illegality under § 812(e) of the Internal Revenue Code of 1939 (Cl. Tr. 85-6). The trial court overruled the demurrer without opinion (Cl. Tr. 89).

In defendants' answer filed May 3, 1960, the illegality under the Federal Estate Tax law was reasserted at length as defendants' first affirmative defense. (Cl. Tr. 97-101; see Opinion on Appeal, App. 6.) Petitioners alleged in substance that the purpose of the secret trust was to permit a false claim to the marital deduction under the Federal Estate Tax law and that this illegality barred any enforcement of the trust.

This issue of illegality under the federal law was reiterated in the defendants' pre-trial statement (Cl. Tr. 165) and in the court's pre-trial order (Cl. Tr. 150).

The trial court, in its Opinion (App. 16-68), Findings of Fact and Conclusions of Law (Cl. Tr. 352-463; 517-528) and Judgment (Cl. Tr. 465-491; 529-571), held that the trust should nevertheless be enforced. The fact that the parties acted on advice of counsel without any deliberate intent to violate the law was one of the factors which influenced the court's decision. The trial court was also impressed with the view that the rules against enforcement of illegal transactions were inapplicable to transactions involving evasion of Federal taxes. (See Opinion of trial court, App. 48-51.)

Again, on Petitioners' appeal to the California District Court of Appeal the illegality issue under the Federal Es-

tate Tax law was the primary issue raised by Petitioners. In accordance with California practice, the issue was raised in Petitioners' Appellate Brief. (See quotations from Brief, App. 69-70.) The California District Court of Appeal, in its Opinion, recognized that this was the principal issue presented for its determination (App. 6).

The District Court of Appeal, in affirming the Judgment of the trial court, relied upon the finding of good faith in acting on advice of counsel as a sufficient answer to the illegality (App. 7-10), although it agreed that:

> "There is no doubt that the objective of the parties in entering into the agreement was to obtain the marital tax deduction, while still carrying out Mrs. Pendleton's wishes with respect to the disposition of the Folger stock." (App. 6)

The issue of illegality under the Federal Estate Tax law was again raised as the principal issue in Petitioners' Petition for a Hearing in the California Supreme Court. (See excerpts from Petition for California Supreme Court Hearing, App. 75-76.) The California Supreme Court denied the Petition for Hearing without comment (App. 17).

The third Federal question presented is whether or not it was actually improper to take the marital deduction under the circumstances of the case. This question has been raised implicitly throughout the case in that a necessary element of Petitioners' contention that the court should not enforce the trust because of illegality under Federal law is that there was in fact some illegality. Thus, throughout the case, Petitioners have taken the position that Mrs. Pendleton was instrumental in limiting her husband to a terminable interest and it was therefore illegal to take the marital deduction.

No serious question was ever raised as to the correctness of this position, at least until the decision of the California

District Court of Appeal. Although the Court's Opinion is not clear on the point, it appears possible that the Court may have based its judgment in part upon the proposition that that no illegality under the Federal Estate Tax law was necessarily involved in the transaction. The court, in its Opinion, refers to the advice of counsel to the effect that Col. Pendleton and Howard Platt, as legatees under Mrs. Pendleton's will could make any agreement between themselves as to the ultimate disposition of the property which they might desire, and that so long as the limitation of Col. Pendleton to a life estate did not "emanate" from Mrs. Pendleton, this would not affect the allowability of the marital deduction under the Federal Estate Tax law (App. 2). The court, in referring to the objective of the parties of obtaining the marital deduction on this basis states:

> "As an abstract matter, this is not an illegal objective." (App. 6)

The facts of the case as found by the trial court, however, were that Mrs. Pendleton made her will with the outright bequest in reliance upon the oral and written agreement of Col. Pendleton and Howard Platt that the property would be placed in a trust in which Col. Pendleton would be limited to a life estate. (See *supra*, p. 7.) The District Court of Appeal did not, in any way modify these findings, and we should state frankly that we do not believe that the Court actually intended to hold that the marital deduction could properly be taken under these circumstances. It has appeared desirable to present the question, however, in order to cover all possible explanations of the Court's decision. If the Court's Opinion is to be construed as holding that under these facts the marital deduction could properly be taken in the determination of Federal Estate Taxes, then this third Federal question has definitely been brought into the case.

In Petitioners' Petition to the District Court of Appeal for a Rehearing, Petitioners pointed out that Mrs. Pendleton had been instrumental in placing restrictions on the bequest to her husband, and Petitioners asked for clarification of the court's Opinion on this point. (See quotation from Petition for Rehearing, App. 70-75.) The District Court of Appeal denied the Petition for Rehearing without comment (App. 16).

This question arising under the Opinion of the District Court of Appeal was also brought to the attention of the California Supreme Court in Petitioners' Petition for a Hearing by that court. (See quotation from Petition for Hearing, App. 75-76.) The California Supreme Court denied the Petition without comment (App. 17).

Respondents, in their reply to the Petition for Hearing by the California Supreme Court, agreed with Petitioners' contention that under the facts of the case the restriction of Col. Pendleton to a life estate was a limitation placed by Mrs. Pendleton. (See quotation from Respondents' Reply, App. 76-77.) This, Respondents agreed, was the whole basis of the case which the District Court of Appeal had before it to decide. Thus, if the District Court of Appeal Opinion is to be construed as holding that since Col. Pendleton and Howard Platt also had a written agreement between them, it was legal to take the marital deduction regardless of the part played by the decedent, then the third Federal question, under the Federal Estate Tax law, is presented.

REASONS FOR GRANTING THE WRIT

The Questions Presented are Federal Questions.

Many decisions of this court have demonstrated that when Federal law is involved it is the province of this court not only to construe its express provisions, but also to determine

the extent and nature of the legal consequences of any violation, even though the transaction is between private litigants and on its face presents nothing more than a local question. Thus, the Federal aspect of a transaction involving Federal law is not confined to the construction and application of the express provisions of the law. It extends to all consequential phases, for here the policy of the law and the intent of Congress may be just as important as its express provisions.

Sola Electric Co. v. Jefferson Electric Co., 317 U.S. 173 (1942). This was an action to recover royalties and enforce a patent licensing agreement. The defendant contended that the agreement, which contained a price fixing clause, was in violation of the Sherman Act. Plaintiff argued that defendant was estopped to assert this defense. This Court held that the question of estoppel was a matter of Federal law to be decided in accordance with Federal policy. The Court stated:

> "When a federal statute condemns an act as unlawful, the extent and nature of the legal consequences of the condemnation, though left by the statute to judicial determination, are nevertheless federal questions, the answers to which are to be derived from the statute and the federal policy which it has adopted. To the federal statute and policy, conflicting state law and policy must yield."
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> * * * * * * *
>
> "A state by applying its own law of specific performance may not compel the performance of a contract contemplating violation of the federal land laws. *Anderson v. Carkins*, 135 U.S. 483, 34 L.Ed. 272. Similarly this Court has declared that anyone sued upon a contract may set up as a defense that it is in violation of the Sherman Act. *E. Bement & Sons v. National Harrow Co.*, 186 U.S. 70, 88, 46 L.Ed. 1058, 1067. And it has proceeded on the assumption that whether the parties to

> an agreement in violation of the Act are in pari delicto is a question of federal, not state, law. *Harriman v. Northern Securities Co.*, 198 U.S. 244, 49 L.Ed. 739; *Eastman Kodak Co. v. Southern Photo Materials Co.*, 273 U.S. 359, 376-378, 71 L.Ed. 684, 690, 691. * * *" (317 U.S. at 176, 177)

See also *Katzinger v. Chicago Metallic Mfg. Co.*, 329 U.S. 394 (1947).

MacGregor v. Westinghouse Elec. & Mfg. Co., 329 U.S. 402 (1947), (reversing Pennsylvania Supreme Court on certiorari).

Similarly, questions of enforceability of transactions which involve some element of illegality under Federal law are Federal questions. This, of course, is obvious where Congress has legislated specifically as to the consequences of illegality. But whether Congress has been specific on the subject or not, the effect of illegality under Federal law is still a Federal question.

Bruce's Juices v. American Can Co., 330 U.S. 743 (1947). This was an action in the Florida state courts to enforce renewal promissory notes. The defendant contended that the notes were illegal and unenforceable because they arose out of sales by the plaintiff which were discriminatory in violation of the Robinson-Patman Act. This Court heard the case on certiorari, and held that this question of illegality was a Federal question. The Court stated:

> "The federal question which survives proceedings in the Florida state courts is whether renewal notes representing the purchase price of goods sold and delivered are uncollectible if it is found that the vendor violated the Robinson-Patman Act". (330 U.S. at 744)

Kelly v. Kosuga, 358 U.S. 516 (1959). This was an action for the purchase price of fifty cars of onions. The buyer de-

fended on the ground of illegality under the Sherman Act. This Court recognized that the question was a Federal question when it stated:

> "Obviously, state law governs in general the rights and duties of sellers and purchasers of goods, and, while the effect of illegality under a federal statute is a matter of federal law, * * *". (358 U.S. at 519)

A. C. Frost & Co. v. Coeur D'Alene Mines Corp., 312 U.S. 38 (1941). This court, in reversing an Idaho Supreme Court decision on certiorari, held that the effect of illegality under the Securities Act of 1933 was a Federal question.

Deitrick v. Greaney, 309 U.S. 190 (1940), involved enforcement of note given to a bank for a consideration which was illegal under the National Bank Act. The United States Supreme Court stated:

> "A point much discussed in brief and argument, upon the assumption that local law will guide our decision, see *Erie R. Co. v. Tompkins*, 304 U.S. 64, is whether by Massachusetts law * * * [defendant] is precluded from setting up the illegality of the transaction as a defense to his note. But it is the federal statute which condemns as unlawful * * * [defendant's] acts. The extent and nature of the legal consequences of this condemnation though left by the statute to judicial determination, are nevertheless to be derived from it and the federal policy which it has adopted * * *. We have recently held that the judicial determination of the legal consequences which flow from acts condemned as unlawful by the National Bank Act involves decision of a federal, not a state question." (309 U.S. at 200-201)

Awotin v. Atlas Exchange National Bank, 295 U.S. 209 (1935). This was an action in the Illinois state courts against a national bank for breach of an agreement by the bank to repurchase certain bonds. It was contended that this agreement was illegal under the National Bank Act. This Court

granted certiorari. This Court held that the question of enforceability and also the question of plaintiff's right to restitution in the absence of enforcement were Federal questions. See also *Kimen v. Atlas Exchange National Bank*, 295 U.S. 215 (1935).

D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 315 U.S. 447 (1942).

Sage v. Hampe, 235 U.S. 99 (1914), involved a contract for the sale of certain land in Kansas. The land was owned by an Indian patentee under act of Congress which contained certain limitations on transferability of the land. The Kansas Supreme Court had held the contract to be enforceable since the Indian patentee was not a party to the contract and the Congressional limitations did not apply directly to the contract. Justice Holmes, speaking for this Court, held that even though the parties were not expressly subject to the Congressional restrictions, still the contract was illegal because of the tendency to promote illegality under the Federal act. Justice Holmes further held that this was a Federal question. His Opinion is certainly applicable here:

> "The only doubt open in the present position of the case is whether the ground upon which we hold the contract unenforceable is not a matter of common law, which we may think that the Kansas courts ought to apply, but which is not open to review here. The case at first sight seems like those in which a state decides to enforce or not to enforce a domestic contract notwithstanding or because of its tendency to cause a breach of the law of some other state. [Citations omitted] But the policy involved here is the policy of the United States. It is not a matter that the states can regard or disregard at their will." (235 U.S. at 106)

It is thus clear that where illegality under Federal law is involved, the effect of such illegality upon enforceability of private transactions is a question of the policy of the Federal law to be passed upon by this court. It is also clear that the existence of the Federal question is not dependent upon its being labeled as such. It is the inherent nature of the question which controls. (See *Deitrick v. Greaney* 309 U.S. 190 (1940) *supra* p. 15.)

The third question reviewed above is also clearly a Federal question. It involves the construction of the express provisions of the Internal Revenue Code § 812(e)(1)(B) concerning terminable interests. If the California District Court of Appeal has held that under the circumstances of this case the bequest to the surviving spouse was not a terminable interest, then certainly we have a question which should be decided on a uniform basis for the whole country without regard to how any particular state court might apply its own local law to these facts.

Burnet v. Harmel, 287 U.S. 103 (1932);
Lyeth v. Hoey, 305 U.S. 188 (1938);
United States v. Pelzer, 312 U.S. 399 (1941);
Rogers' Estate v. Helvering, 320 U.S. 410 (1943).

The Question of Enforceability of Tax Evasion Transactions Is of Paramount Importance and Should Be Decided by This Court.

The basic issue in this case is whether or not court enforcement should be granted to a transaction entered into for the purpose of accomplishing an evasion of Federal taxes. An incident of this question is the weight to be attached to the subjective good faith of the parties in the patently evasive transaction.

Our research has revealed no case in which this court has decided these illegality question in the tax field. This court has, however, had frequent occasion to enunciate

the general principles concerning court enforcement of illegal transactions in other areas of the law. The general principle that the courts should not enforce illegal transactions or transactions entered into for an illegal purpose has been fully recognized. The importance of discouraging illegal transactions far outweighs the importance of adjusting the private equities of the parties. Thus, when a party must rely upon a transaction tainted with illegality in order to establish his case, the courts cannot help him. The policy is "hands off".

Thus, in *McMullen v. Hoffman*, 174 U.S. 639 (1899), a case which arose out of a collusive bidding arrangement, the Court stated:

> "The authorities from the earliest time to the present unanimously hold that no court will lend its assistance in any way towards carrying out the terms of an illegal contract. In case any action is brought in which it is necessary to prove the illegal contract in order to maintain the action, courts will not enforce it, nor will they enforce any alleged rights directly springing from such contract."
>
> * * * * * * *
>
> "The court refuses to enforce such a contract, and it permits defendant to set up its illegality, not out of any regard for the defendant who sets it up, but only on account of the public interest. It has been often stated in similiar cases that the defense is a very dishonest one, and it lies ill in the mouth of the defendant to allege it, and it is only allowed for public considerations and in order the better to secure the public against dishonest transactions. To refuse to grant either party to an illegal contract judicial aid for the enforcement of his alleged rights under it tends strongly towards reducing the number of such transactions to a minimum. The more plainly parties understand that when they enter into contracts of this nature they place themselves outside the protection of the law, so far as that protection consists in aiding them to enforce such

> contracts, the less inclined will they be to enter into them. In that way the public secures the benefit of a rigid adherence to the law." (174 U.S. at 654, 669)

In *Dent v. Ferguson*, 132 U.S. 50 (1889), the Court refused to enforce a secret trust under which a grantee of property conveyed in fraud of creditors had agreed to return the property to the grantor. The court stated:

> "It * * * involves a secret trust for the return to himself of property of which such creditors have the immediate right of sale. The law does not countenance any such transaction, but leaves both parties in the position where they have placed themselves." (132 U.S. at 67)

Application of this rule of nonenforcement is not dependent on express statutory language to the effect that violative transactions shall not be enforceable.

United States v. Mississippi Valley Generating Co., 364 U.S. 520, 563 (1961) quoted *infra*, page 21.

Hazelton v. Sheckels, 202 U.S. 71 (1906) (Contract against public policy)

Application of the rule against nonenforcement is not confined to transactions which expressly call for a violation of the law. The mere tendency to promote illegality or a purpose to accomplish an illegal objective provide adequate reason for court refusal to enforce. In *Sage v. Hampe*, 235 U.S. 99 (1914) (reviewed *supra*, page 16), the statute involved was an act of Congress which barred any conveyance of land by an Indian patentee for a period of 25 years without approval of the Secretary of Interior. This Court held that under this law a contract for the sale of the land by a seller who did not own the land and who was not directly subject to the congressional act, was illegal

because of the tendency which the contract would induce to attempt to get the land away from the Indian owner in violation of the intent of Congress. Justice Holmes, speaking for the Court, stated:

> "And more broadly, it long has been recognized that contracts that obviously and directly tend in a marked degree to bring about results that the law seeks to prevent cannot be made the ground of a successful suit. Providence Tool Co. v. Norris, 2 Wall. 45, 17 L. ed. 868; Trist v. Child (Busk v. Child) 21 Wall. 441, 22 L. ed. 623; Oscanyan v. Winchester Repeating Arms Co., 103 U. S. 261, 26 L. ed. 539; Fuller v. Dame, 18 Pick. 472. It appears to us that this is a contract of that class. * * *"
>
> "It is true that later statutes in force when the contract was made allowed a conveyance with the approval of the Secretary of the Interior. * * * The Kansas court laid these statutes on one side, and in our view also they do not affect the case. The purpose of the law still is to protect the Indian interest, and a contract that tends to bring to bear improper influence upon the Secretary of the Interior, and to induce attempts to mislead him as to what the welfare of the Indian requires, are as contrary to the policy of the law as others that have been condemned by the courts." (235 U.S. at 105)

Woodstock Iron Co. v. Richmond & Danville Extension Co., 129 U.S. 643 (1889). This Court stated:

> ". . . agreements like the one in this case; . . . are against public policy because of their corrupt tendency, whether lawful or unlawful means are contemplated or used in carrying them into execution. 'The law, . . . looks to the general tendency of such agreements; and it closes the door to temptation by refusing them recognition in any of the courts of the country.'" (129 U.S. at 663)

See also *Weil v. Neary*, 278 U.S. 160 (1929), quoted *infra*, pages 22-23.

In the great majority of the illegality cases the courts' ruling against enforcement is based upon the actual illegality inherent in the transaction or in its purpose, without regard to the subjective good or bad faith of the parties. There have, however, been some cases before this court in which a party has contended that the usual rules of illegality should not be applied because the parties acted in good faith and without any evil fraudulent intent. Thus, in *United States v. Mississippi Valley Generating Co.*, 364 U.S. 520 (1961), involving a government contract in which there was a conflict of interest on the part of one of the negotiators, this Court held:

> "Having determined that Wenzell's activities constituted a violation of Section 434, we must next consider whether Wenzell's illegal conduct renders the contract unenforceable. It is true that Section 434 does not specifically provide for the invalidation of contracts which are made in violation of the statutory prohibition. However, that fact is not determinative of the question, for a statute frequently implies that a contract is not to be enforced when it arises out of circumstances that would lead enforcement to offend the essential purpose of the enactment. e. g., Miller v. Ammon, 145 U.S. 421, 36 L ed 759, 12 S Ct 884; Bank of United States v. Owens (US) 2 Pet 527, 7 L ed 508; 6 Williston, Contracts (rev ed 1938) § 1763.
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> * * * * * * *
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> "The Court of Claims was of the opinion that it would be overly harsh not to enforce this contract, since the sponsors could not have controlled Wenzell's activities and were guilty of no wrongdoing. However, we think that the court emphasized the wrong considerations. Although nonenforcement frequently has the effect of punishing one who has broken the law,

"its primary purpose is to guarantee the integrity of the federal contracting process and to protect the public from the corruption which might lie undetectable beneath the surface of a contract conceived in a tainted transaction. Cf. Crocker v. United States, 240 US 74, 80, 81, 60 L ed 533, 537, 36 S Ct 245. It is this inherent difficulty in detecting corruption which requires that contracts made in violation of Section 434 be held unenforceable, even though the party seeking enforcement ostensibly appears entirely innocent. Cf. Hazelton v. Sheckels, 202 US 71, 79, 50 L ed 939, 941, 26 S Ct 567, 6 Ann Cas 247." (364 U.S. at 563, 564)

United States v. Trans-Missouri Freight Association, 166 U.S. 290 (1897), a case arising under the Sherman Act:

"For these reasons the suit of the government can be maintained without proof of the allegation that the agreement was entered into for the purpose of restraining trade or commerce or for maintaining rates above what was reasonable. The necessary effect of the agreement is to restrain trade or commerce, no matter what the intent was on the part of those who signed it." (166 U.S. at 342)

Harriman v. Northern Securities Co., 197 U.S. 244 (1905), also involved the Sherman Act. The Court stated:

"We regard the contention that complainants are exempt from the doctrine *in pari delicto* because the parties acted in good faith and without intention to violate the law as without merit. With knowledge of the facts and of the statute, the parties turned out to be mistaken in supposing that the statute would not be held applicable to the facts." (197 U.S. at 298)

Weil v. Neary, 278 U.S. 160 (1929), a case involving an agreement to divide fees in a bankruptcy matter:

"The chief argument that is pressed upon us to declare the contract valid and to sustain the judgment

based upon it is the success with which the plaintiff is found to have worked out a useful settlement of the estate for the benefit of the creditors, and the absence of any finding or showing that there was actual fraud. But this is not a sufficient answer to the charge of illegality. The contract is contrary to public policy—plainly so. What is struck at in the refusal to enforce contracts of this kind is not only actual evil results but their tendency to evil in other cases. Even if the ultimate results in the management of the Thompson estate were good that could be no excuse for a contract plainly illegal, because tending to produce the recognized abuses which follow fraud and disloyalty by agents and trustees. Enforcement of such contracts, when actual evil does not follow, would destroy the safeguards of the law and lessen the prevention of abuses. Providence Tool Co. v. Norris, 2 Wall. 45, 17 L. ed. 868; Woodstock Iron Co. v. Richmond & D. Extension Co. 129 U.S. 643, 32 L. ed. 819, 9 Sup. Ct. Rep. 402; Oscanyan v. Winchester Repeating Arms Co. 103 U.S. 261, 26 L.ed. 539; Maguire v. Corwine, 101 U.S. 108, 25 L.ed. 899; Connors v. Connolly, 86 Conn. 641, 45 L.R.A. (N.S.) 564, 86 Atl. 600; Richardson v. Crandall, 48 N.Y. 348; Palmbaum v. Magulsky, 217 Mass. 306, 308, 104 N.E. 746, Ann. Cas. 1915D, 799." (278 U.S. at 173)

There are numerous decisions of this court as to just how these basic principles on illegality should be applied in particular fields of Federal law. (See cases reviewed at pages 13 to 16, *supra*, arising under Sherman Act, Robinson-Patman Act, Securities Act of 1933, and National Bank Act.) The rules applicable in one field are not necessarily conclusive, however, as to the proper rules in other fields. See for example *A. C. Frost & Co. v. Coeur D'Alene Mines Corp.*; 312 U.S. 38 (1941) in which non-enforcement would have hindered rather than helped the purposes of the Securities Act of 1933. In each field this court must consider the

policy and purpose of the enactment in question and the intent of Congress, together with the circumstances of the particular case, in establishing principles as to what transactions are and what transactions are not enforceable. Compare also *Bruce's Juices v. American Can Co.*, 330 U.S. 743 (1947) *supra*, p. 14.

So far as we have been able to ascertain, this court has never made any corresponding determination under the Internal Revenue Code. The Internal Revenue Code is probably the most important law we have, both from the standpoint of government revenues and from the standpoint of the number of persons affected. "No other branch of the law touches human activities at so many points." *Dobson v. Commissioner*, 320 U.S. 489, 494-495 (1943). But on this very vital question of enforceability of Federal tax evasion transactions, this court has made no adjudication.

We should point out that we are not here concerned with some incidental violation of the revenue laws. In the present case the whole purpose of the secret trust for which enforcement is sought was to accomplish an unlawful evasion. Decisions involving perfectly legal transactions where there may be some incidental violation of the tax law involved are consequently inapplicable. (Compare, for example, *Cole v. Ralph*, 252 U.S. 286, 293 (1920), in which failure to affix revenue stamps did not invalidate a conveyance made for a perfectly legal purpose.

Decisions of the state courts have been of little assistance in solving the enforceability question where the actual purpose is Federal Tax evasion. As a matter of fact, there is a conflict. On the one hand we refer to the decision of the California District Court of Appeal in the instant case. We refer also to *Hansen v. Bear Film Company*, 28 Cal. 2d 154, 168 P. (2d) 946 (1946), in which the California Supreme Court said in a suit to enforce a resulting trust:

". . . if the transaction resulted in evasion under the federal taxing statutes, that is an exclusive concern of the federal authorities." (28 Cal. 2d at 176; 168 P. (2d) at 960.)

See also *Farber v. John Aquino Sons*, 3 N.Y. Supp. (2d) 236, 253 App. Div. 600 (1938);

Christopherson & Kiaer v. U. S. Navigation Co., 202 N.Y. Supp. 902, 121 Misc. 778 (1923).

On the other hand, decisions in other states have treated a purpose to evade Federal taxes as grounds for court refusal to enforce a transaction. Thus, in *Shaw v. Addison*, 239 Iowa 377, 28 N.W.2d 816 (1947), the court refused to enforce a trust created for the purpose of evading Federal* income tax. The court stated:

"Plaintiff, as heir of the donor, had no rights superior to those of the donor at the time of his death. The transfer which has for its object and purpose the evasion of taxation is analogous to transfers to defraud creditors about which more will be said in the next division of this opinion. In both cases the parties are in pari delicto and no relief will be granted the transferor in equity but the law will leave them where it finds them. The equitable maxim 'he who comes into equity must come with clean hands' governs the court's action. No resulting trust, that a court of equity will enforce, is established in favor of the transferor, or his successor upon proof of a transfer made for the purpose of evading tax." (28 N.W.2d at 826)

See also *Creekmore v. Chitwood*, 7 Bush (70 Ky.) 317 (1870).

Collins v. Becklenberg, 236 Ill. App. 324 (1925);

Curran v. Down, 3 Mo. App. 468 (1877).

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*The transfers in this case alleged as the basis for the trust were in 1922 and 1929 prior to the enactment of the Iowa income tax law. (Iowa Acts 1933-34 Ex. Sess. (45 G. A.) ch. 82.) Hence, the income taxes referred to were exclusively federal.

Congress has not provided any clear-cut answer to the question. Congress has provided criminal sanctions (e.g., Internal Revenue Code of 1954, 26 U.S.C. §§ 7201-7215) and civil penalties (e.g., 26 U.S.C. § 6653) for various types of violations. In isolated situations, largely where the purpose of the tax is regulatory, Congress has made specific provisions for forfeitures or for the application of the law to private transactions. For example, under the 1954 Code:

26 U.S.C. § 4706, 4714 (Forfeiture of narcotics);

26 U.S.C. § 4853 (b) (Sale of cotton futures—specific prohibition intended; See *Hubbard v. Louy*, 226 Fed. 135, 137 (S.D.N.Y. 1915);

26 U.S.C. § 5612, 5613 (Alcoholic Beverage forfeitures);

26 U.S.C. § 7302 (No property rights in property used for violation—See *U.S. v. Dixon*, 347 U.S. 381 (1954))

26 U.S.C. § 7341(a) (Voiding debts incurred for purchase of property sold with intent to avoid tax.)

Congress has not, however, legislated on the general subject of enforceability of tax evasion transactions, and our review of the legislative history of the above special provisions has not provided any definite clue as to the intent of Congress on the general question. It could be argued that the various specific laws which Congress has enacted preclude any broader congressional intent on the subject. We submit that it is much more probable, however, that the congressional intent is that the courts should apply the established general rules of illegality to tax evasion transactions and refuse enforcement. The tax laws, although sometimes penal in their nature, are to be construed liberally for the protection of the revenues.

United States v. Ryan, 284 U.S. 167, 172 (1931);
Smythe v. Fiske, 23 Wall. (90 U.S.) 374 (1874);
United States v. Stowell, 133 U.S. 1, 12 (1890).

Our tax structure is based primarily on securing a full and fair disclosure by the taxpayer in his tax return.

Spies v. United States, 317 U.S. 492, 495 (1943);
Helvering v. Mitchell, 303 U.S. 391, 399 (1938);
Balter, "Tax Fraud and Evasion" p. 1.4 (3rd Ed. 1963).

In many countries this just doesn't work. Cheating the tax collector is considered to be fair game. In the United States there is a fair degree of cooperation from at least the majority of taxpayers, but evasion continues to be a serious threat to the system.

"* * * evasion practiced by the small minority of taxpayers breeds disrespect for the tax laws on the part of the great majority who attempt to cut square corners with the Government." (Mortenson, "Federal Tax Fraud Law", p. v (1958)).

See also Balter, "Tax Fraud and Evasion", p. 1.4 (3d Ed. 1963).

Paul, "Taxation for Prosperity", p. 287 (1947).

The significance of subjective good faith must also be considered in the light of these factors. The several cases reviewed *supra*, p. 21 to p. 23 demonstrate that on illegality questions generally good faith is no answer; that the importance of discouraging illegality is such that the Courts cannot afford to get bogged down on the always difficult question of subjective intent.

Should these rules concerning illegality be any more relaxed in the tax evasion field? To what extent does advice

of counsel* in an obviously evasive transaction serve to insulate the taxpayer from the normal consequences of his acts? Certainly it is not a complete shield.

Harry Feldman, 34 B.T.A. 517 (1936);

Coates v. Commissioner, 234 F. (2d) 459 (8th Cir. 1956);

Hermax Co. Inc., 11 T.C. 442 (1948) affirmed *per curiam* 175 F. (2d) 776 (3rd Cir. 1949).

Here again on this good faith issue Congress has not provided any definite guide. Congress has provided that for the most stringent sanction, the criminal prosecution, a showing of willfulness—"evil intent"—is required (*Spies v. United States*, 317 U.S. 492 (1943)). This of course does not mean that the same requirement should be applicable to the purely civil sanction of unenforceability.

We respectfully submit that the reasons why courts refuse enforcement of transactions tainted with illegality are fully applicable in the tax evasion field; and that this is what Congress has intended.

The Marital Deduction Could Not Be Properly Claimed.

The facts of the case are that Mrs. Pendleton made her will in reliance upon her husband's promise to limit his bequest to a life estate and to enter into a written agreement for this purpose. This was the finding of the trial court. It was not modified by the District Court of Appeal and it is therefore controlling as to the facts of the case.

*We should point out that the parties did not follow the advice of counsel. Counsel advised that it would be proper to take the marital deduction so long as no restrictions on the outright bequest to Col. Pendleton emanated from Mrs. Pendleton; but the restrictions which were placed did emanate from Mrs. Pendleton.

United States v. Knott, 298 U.S. 544, 548-549 (1936);
Brainard v. Hubbard, 79 U.S. 1, 9-10 (1871).

It requires no citation of specific authority to demonstrate that under these circumstances the interest which Col. Pendleton received as surviving spouse, as limited by the restrictions which the decedent placed, was terminable so that the marital deduction could not properly be taken. For tax purposes the substance of a transaction is far more important than its form. (See *Gregory v. Helvering*, 293 U.S. 465 (1935)) Specific authority does however exist on the point.

See Treasury Regulations quoted *supra*, pp. 4-5;
Lindsey v. U. S., 167 Fed. Supp. 136 (D. Md. 1958).

If the District Court of Appeal decision is to be construed as holding that it was proper to claim the marital deduction under the circumstances of the case, then such holding is certainly contrary to the clearly expressed Congressional intent in § 812(e)(1)(B) (quoted *supra*, p. 4) that terminable interests are not deductible. If so construed, the District Court of Appeal decision would be a very dangerous precedent in anything as far reaching in its application as the marital deduction under the Federal Estate Tax Law.

We must state again that we do not believe that the District Court of Appeal intended to rule that the marital deduction was properly taken. We present the point, however, in order to cover all possible explanations of the court's decision.

The Specific Issue Involving Evasion of the Marital Deduction Provisions of the Estate Tax Law Is Itself a Problem of Far Reaching Consequence.

The marital deduction, provided for by an amendment of the Federal Estate Tax Law in 1948, opens a fertile field for

tax evasion through the use of a secret trust of the type which respondents are here seeking to enforce. The estate of a married decedent owning separate property is allowed a deduction up to one-half of the "gross estate" for property transferred to a surviving spouse. The purpose of this deduction is to place separate property and community property on approximately equal footing for Federal Estate Tax purposes.

Jackson v. United States, ... U.S. ....., 32 L.W. 4222 (March 23, 1964);

Senate Report No. 1013 (3/16/48), accompanying H.R. 4790 [Revenue Act of 1948], 80th Cong., 2d Sess., reproduced at 2 U. S. Code Cong. Serv. (1948) 1163, at 1190;

4 Mertens, "Law of Federal Gift and Estate Taxation", (1959), p. 438.

It was not the intent of Congress however that property should in this manner escape taxation in the estates of both spouses. Even community property would not have this advantage. In order to insure that property for which the marital deduction was taken would not have the added benefit of being left out of the estate of the surviving spouse it was necessary to require that marital deduction property be left to the spouse either outright or with a general power of appointment which would subject it to estate taxes in the estate of the surviving spouse.

Senate Report No. 1013 (3/16/48), *supra*, 2 U.S. Code Cong. Serv. (1948) 1163, at 1190;

4 Mertens, *supra*, p. 440.

If it is possible through the secret trust arrangement which the parties here adopted to nullify the terminable

interest limitations, then a wide loophole for tax evasion is presented.

We are not here concerned with an isolated problem under the Internal Revenue Code. The most recent available figures, for 1961, will demonstrate its importance. In that year 64,538 Federal Estate Tax Returns were filed. On 30,738 of these, the marital deduction was claimed. The total gross estate shown on all returns was $14,622,073,000. The total deduction from the gross estate claimed on account of the marital deduction was $2,795,891,000. This deduction was more than all other deductions combined. (Internal Revenue Service Publication No. 406 (Nov. 13, 1963) "Statistics of Income — 1960, Fiduciary, Gift, and Estate Tax Returns Filed During 1961", pp. 46, 48).

It becomes apparent that over a period of years there are hundreds of thousands of testators who have faced or will have to face the same dilemma as that which confronted Mrs. Pendleton in the present case. On the one hand, there is a desire to limit the surviving spouse to a life estate so as to insure ultimate distribution to other beneficiaries designated by the testator. On the other hand, there is also a desire to minimize taxes by utilizing the marital deduction. Under the law which Congress has enacted testators with this problem must make a choice. They may accomplish one objective or the other. They cannot legally accomplish both.

There will certainly be a strong temptation on the part of many of these testators to attempt to accomplish both objectives through a secret trust of the same type as that utilized by Mrs. Pendleton. There should be no encouragement provided for those who may be so tempted. This certainly is a situation in which the established rules against enforcement of transactions tainted with illegality should apply.

CONCLUSION

We respectfully submit that the foregoing questions, involving as they do the very basic question of the effect of illegality under the Internal Revenue Code and the more specific question concerning the use of the secret trust device in evasion of Federal Estate taxes, should have the attention of this court.

Dated: April 17, 1964

Respectfully submitted

EDWIN S. PILLSBURY
155 Montgomery Street
San Francisco 4, California
Attorney for Petitioners

DAVID C. DUNLAP
PILLSBURY & DUNLAP
155 Montgomery Street
San Francisco 4, California

PAUL I. MYERS, JR.
681 Market Street
San Francisco 5, California
Of Counsel

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No. 1023

In the Supreme Court of the United States

WELLS FARGO BANK and A. B. NEIL, JR.,
as Executors of the Will
of Louis L. Pendleton, Deceased,

Petitioners,

vs.

HOWARD C. PLATT, ROBERT C. PLATT, a minor,
and MARILYN A. PLATT, a minor,
by his and her Guardian Ad Litem,
Howard C. Platt,

Respondents.

Appendix to Petition for Writ of Certiorari to the District Court of Appeal of the State of California First Appellate District

EDWIN S. PILLSBURY
155 Montgomery Street
San Francisco 4, California

Attorney for Petitioners

DAVID C. DUNLAP
PILLSBURY & DUNLAP
155 Montgomery Street
San Francisco 4, California

PAUL I. MYERS, JR.
681 Market Street
San Francisco 5, California

Of Counsel

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Appendix A

In the District Court of Appeal of the State of California
First Appellate District—Division Two

1 Civ. No. 2938

Howard C. Platt, Robert C. Platt, a minor, and Marilyn A. Platt, a minor, by his and her Guardian ad Litem, Howard C. Platt,

Plaintiffs and Respondents,

vs.

Wells Fargo Bank American Trust Company, a corporation, and A. B. Neil, Jr., executors of the Estate of Louis L. Pendleton, deceased,

Defendants and Appellants.

OPINION

The trial court impressed a trust in favor of plaintiffs upon certain corporate stock. Defendants have appealed, contending that such relief is barred by the defense of illegality and unclean hands. The facts will be stated in the light most favorable to respondents.

Gladys Platt Pendleton executed her last will on October 15, 1949. After providing for certain specific bequests, the residue was left to her husband, Louis L. Pendleton, and her nephew, Howard C. Platt, in equal shares.

The residue consisted almost entirely of stock in the Folger Coffee Company, which had come to Mrs. Pendleton by inheritance. She wanted all of it to go to her nephew and his children, thus keeping it in what she referred to as the "Platt Blood Line." The will did not express this wish. The reason therefor follows.

In 1949, Mrs. Pendleton had directed her attorney, Herbert E. Wenig, to prepare a new will. While Wenig was in the process of doing so, Pendleton happened to receive a pamphlet distributed by a New York bank. It discussed the new marital tax deduction provided for in the Federal Revenue Act of 1948. He took this to Wenig's office and asked him about the advisability of drafting the will with this deduction in mind. Wenig told him that he would look into the matter.

Under the provision in question, up to one-half of a deceased spouse's estate is exempt from federal estate tax if it is left to the surviving spouse either outright or, if such portion is left in trust, the surviving spouse is entitled to all the income for life and has an unrestricted power of appointment.

Wenig reached the conclusion that, so long as any limitations or restrictions on the bequest of the Folger stock to Pendleton did not emanate from Mrs. Pendleton, Platt and Pendleton could make any agreement that they wanted to as between themselves with respect to the property being bequeathed to them, and that such an agreement would not affect the right to the marital deduction.

Wenig so advised all of the parties and Mrs. Pendleton expressed herself as being willing to rely upon Pendleton to carry out her wishes. Pendleton assured her that he would do so. Pendleton and Platt both knew what these wishes were, having discussed them with her on many occasions.

Mrs. Pendleton then executed the will of October 15, 1949, naming Pendleton and Platt as executors. Later, on the same day, Pendleton and Platt made a written agreement between themselves that all of the residue distributed to them would be placed in an irrevocable trust with themselves

as trustees; that two-thirds of the net annual income from the trust estate would go to Pendleton and one-third to Platt; that on Pendleton's death, the trust would terminate as to two-thirds of the corpus, which would then go to Platt, and the other one-third of the corpus would remain in trust, with Platt's two children as the beneficiaries.

This agreement is sometimes referred to herein as the "trust agreement." Wenig had prepared the will and the agreement and had advised Pendleton and Platt that the arrangement provided for therein was perfectly legal and proper and would still allow Pendleton to claim the marital deduction for the purpose of the estate tax. Pendleton and Platt both accepted this advice and relied upon it in good faith.

Pendleton and Platt also made another agreement at the same time. This referred to a parcel of commercial realty held in joint tenancy by Mrs. Pendleton and Pendleton. This property had been purchased with Mrs. Pendleton's funds and Pendleton agreed that, upon her death, he would convey a one-third interest therein (except a designated portion of the southwest corner) to Platt.

Later, Mrs. Pendleton expressed the wish that, upon Pendleton's death, this entire parcel (less the excepted portion) should go to Platt. Pendleton agreed to this but it was not put in writing until January 6, 1960, shortly after Mrs. Pendleton's death. This agreement provided that, when Pendleton received the property as the surviving joint tenant, he would convey it (less the excepted portion) to Platt in trust, Platt to pay him two-thirds of the net annual income therefrom and the trust to terminate upon Pendleton's death. On November 1, 1951, Pendleton executed and delivered a deed of said property to Platt.

The agreements and the deed were intended by Pendleton and Platt to carry out the desires of Mrs. Pendleton with respect to the Folger stock and the commercial real property.

Mrs. Pendleton died on January 3, 1950. Pendleton and Platt employed Wenig as the attorney for the estate and the will of October 15, 1949 was admitted to probate on February 3, 1950.

During the course of administration, Wenig prepared the federal estate tax return. Schedule M of the return related to the claim of marital deduction. Question 5 thereof reads as follows: "According to the information and belief of such person or persons, has any person other than the surviving spouse asserted (or is such assertion contemplated) a right to any property interest listed on this schedule, other than as indicated under questions (1) and (4)?"

Wenig inserted the answer "No" to this question. He testified that he did so because the agreement between Pendleton and Platt "in no way reduced the interest which Colonel Pendleton received from Mrs. Pendleton's estate. The agreement, in my opinion, created no interest which would be subject to the probate of the estate. I had given careful consideration to the matter at the time of drafting the agreement and checked the authorities and, in my opinion, it created an interest in both Howard [Platt] and the Colonel [Pendleton] only after distribution but . . . it did not create any interest at the time or during the course of probate."

Wenig executed the "Affidavit of Attorney" attached to the return, in which he avers that the return "is a true, correct, and complete statement of all the information respecting the estate tax liability of this estate of which I have any knowledge." Pendleton and Platt thereafter signed the return as executors, relying upon Wenig for its accuracy.

The estate was distributed on January 9, 1952, and Pendleton and Platt received the Folger stock in equal shares. Wenig had advised them that the execution of any formal trust agreement would have to await actual distribution. Such an agreement was never executed. While the record is replete with the causes for the many delays, it is unnecessary to go into detail here. Appellants concede that they "do not question the ultimate decision of the trial court on the issue of limitations and laches."

Pendleton and Platt worked out an interim arrangement for the disbursement of income, payment of taxes, etc., and Platt rendered annual statements to Pendleton for the years 1952 through 1958.

However, the whole matter was brought to a head by a letter from Pendleton's attorney to Wenig, dated May 5, 1959, denying any *legal* obligation on the part of Pendleton to carry out the trust agreement. The letter states that Pendleton was willing to maintain his will bequeathing the Folger stock which he had received from his wife's estate to Platt and his children "on the condition that Howard Platt agrees to maintain his income payments to Col. Pendleton and that Mr. Platt cease trying to *force* Col. Pendleton to place his property in a trust." (Italics added.)

Platt thereupon retained present counsel who, on September 28, 1959, wrote to Pendleton's attorney as follows: "Unless a trust agreement in substantially the form set forth in the enclosure is executed on or before the 2nd day of November, 1959, we will commence litigation to enforce the rights of Mr. Platt and his two minor children." The agreement was not executed.

On November 4, 1959, Platt and his two children commenced this action to impress a trust upon the stock. They also sought to impress a trust upon the Pendleton home property.

On May 3, 1960, Pendleton filed an answer, affirmatively alleging that the agreement between himself and Platt was illegal and unenforceable since the sole purpose thereof was the unlawful and fraudulent evasion of federal estate taxes. By way of cross-complaint, Pendleton sought to cancel his deed of the commercial property to Platt on the ground of undue influence by Platt.

Pendleton died on November 23, 1960, and the executors of his estate were substituted for him. His deposition was read at the (nonjury) trial.

Judgment was rendered in favor of respondents as to the stock but against them as to the home property. Appellants were denied a cancellation of the deed to the commercial property. The home property is not included in this appeal, respondents not having cross-appealed.

Appellants' main contention on appeal is that the trust agreement is illegal and therefore unenforceable because it was entered into with the intent and for the purpose of defrauding the federal government of a portion of the federal estate taxes.

There is no doubt that the objective of the parties in entering into the agreement was to obtain the marital tax deduction, while still carrying out Mrs. Pendleton's wishes with respect to the disposition of the Folger stock. As an abstract matter, this is not an illegal objective.

Likewise, as an abstract matter, it is not illegal for the beneficiaries under a will to make an agreement between themselves as to how they will dispose of their respective legacies when received by them.

However, if Pendleton and Platt entered into the trust agreement with the intent of fraudulently concealing its existence from the federal government for the purpose of obtaining the marital tax deduction, the agreement is illegal

and unenforceable. (12 Cal. Jur. 2d, p. 297, "Effect of Illegality," Contracts § 98.) The result would be the same under the clean hands doctrine. (18 Cal. Jur. 2d, p. 183, "Doctrine of Clean Hands," Equity § 28.)

"Intent" and "purpose" are ordinarily questions of fact to be determined by the trial court. As stated in Boericke v. Weise, 68 Cal. App. 2d 407, 418: "Whether plaintiffs are within the application of the maximum [unclean hands] is primarily a question of fact."

The trial court made findings of fact from which it concluded that neither Mrs. Pendleton, Pendleton, nor Platt acted with any fraudulent intent or purpose and that they relied upon the advice of counsel that what they were doing was in all respects legal and proper.

These findings are supported by substantial evidence and are quite detailed. The substance thereof, as to Platt, is that he was first told of the marital deduction provision on October 10, 1949; that Wenig advised him that this deduction could be claimed and Mrs. Pendleton's wishes as to the disposition of her property could also be carried out if he and Pendleton would execute an agreement providing therefor, after Mrs. Pendleton had signed the will which Wenig was then drafting; that Platt did not at any time have the intent or purpose to fraudulently evade taxes; that he relied and acted upon the advice of Wenig that the proposed arrangement was legal and proper; that after Mrs. Pendleton's death, as co-executor of her estate, he signed the federal estate tax return in reliance upon the advice of Wenig and without any knowledge that there was or might be any false representation contained therein.

Appellants state that they "do not question the trial court's finding of good faith. . . ." This is, of course, merely an acknowledgment of the rule that an appellate court will

not overturn a finding of fact based upon substantial evidence.

Appellants say that it "is immaterial" that "[t]he trial court found that the parties acted in good faith on advice of counsel and did not intend to violate any law." This is so, appellants assert, because "[t]he tax evasion scheme *necessitated* a concealment of the true facts." (Italics ours.)

Respondents point out the inconsistency between appellants' concession as to "good faith" and the charge of "concealment." However, what appellants probably mean to contend is that Wenig's legal opinion as to the right to the marital deduction under the arrangement set up by him is completely worthless and without any legal merit whatsoever; that the object of the trust agreement could therefore only be accomplished by failing to disclose its existence to the federal government; that if the federal government had been advised of the agreement between Pendleton and Platt, there could not be even the slightest doubt that the marital deduction would have been denied.

Appellants make no contention that Wenig acted in bad faith in rendering his opinion to the Pendletons and to Platt. The merit of this opinion is not an issue to be determined by us. The record does not disclose what position the federal government intends to take in this matter, although it was given full notice of this action at the commencement thereof.

Pendleton and Platt left the handling of the marital tax deduction up to Wenig. If it was allowed, so much the better. If it was disallowed, the increased estate tax would have to be paid out of Mrs. Pendleton's estate. Her will contained the express provision that "all federal estate taxes . . . shall be paid out of the residue of my probate estate."

The performance of the trust agreement by the parties was not made dependent or contingent upon the allowance

or disallowance of the marital tax deduction. It is perfectly clear that the parties intended to and did bind themselves with respect to the ultimate disposition of the Folger stock, regardless of the outcome of the tax deduction claim.

Where an agreement (to claim a tax deduction) does not require the parties to do anything illegal in performing it, the good faith of such parties becomes of great importance if, in fact, such agreement is performed in an illegal manner.

In Du Pre v. Bogumill, 173 Cal. App. 2d 406, the court stated, at page 413: "The defendant engaged the attorney to draft the documents and to advise them with reference to the transaction and plaintiff relied upon the representations of the attorney that the contract and the proceeding were proper and plaintiff conducted himself at all times as requested by the defendant. No bad motive and no intent to violate the law appears in anywise upon the part of the plaintiff."

The court quotes with approval from 12 California Jurisprudence 2d 272, section 69, as follows: "If an agreement which does not provide for a method of accomplishing its purpose can be accomplished by any legal method, it must be assumed that such method was contemplated when the contract was made and will be pursued, and it will not be presumed that the parties intended to perform in an illegal manner. Moreover, where a contract can be performed in a legal manner as well as in an illegal manner, it will not be declared void because it was in fact performed in an illegal manner."

However, this last principle does not apply where the one seeking to enforce the contract participates in the illegal performance.

Assuming that Wenig's failure to inform the federal government of the trust agreement amounted to fraud, this does not make Platt a participant therein. The trial court expressly found that Platt had no notice or knowledge of any illegality or impropriety in connection with the filing of the federal estate tax return; that he signed the return as co-executor in reliance upon the advice of counsel that it was in all respects properly filled out; that said counsel was the same counsel who had prepared the will of October 15, 1949 and the trust agreement executed on the same day; that Platt did not attempt to use any transactions involved herein "as a coverup device to conceal facts or to carry out any scheme to evade taxes in the estate of Mrs. Pendleton . . ."

These findings are supported by substantial evidence. In our opinion, the trial court's rejection of the defenses of illegality and unclean hands should be upheld.

As to appellants' contention that Platt exercised undue influence upon Mrs. Pendleton and Pendleton, this merely presents a question of fact which was resolved by the trial court adversely to appellants.

Appellants rely upon the familiar rule that when a confidential relationship exists and the party in whom confidence is reposed obtains some benefit, there is a presumption of undue influence.

However, this presumption is rebuttable and the trial court made detailed findings of fact which completely exonerated Platt from such charge, including the following finding: "[P]laintiff Platt did not exercise any undue influence over Mrs. Pendleton or defendant Pendleton or exercise any control or dominion over Mrs. Pendleton or defendant Pendleton at any time whatever in respect to any matter whatever." These findings are supported by substantial evidence.

Appellants next assert that the trust agreement did not provide for "a definitely ascertained trust corpus" and that the parties should not have been "left free to determine by their own [subsequent] agreement what should constitute the corpus of the constructive trust . . ."

At the time of the execution of the agreement, Pendleton and Platt knew that Mrs. Pendleton's will provided that the residue of her estate was to go to them. They knew that the Folger stock was included in such residue. This stock represented practically the entire estate subject to probate and it was the only asset expressly referred to in the trust agreement.

Pendleton and Platt did not know at the time, of course, that the Folger stock was to be the only asset left in the residue to distribute. For this reason, the trust agreement provided that the trust was to consist of "all the residue distributed to them. . . ." We think that the trust residue was sufficiently identified by the trust agreement.

After distribution of the specific bequests there remained some miscellaneous stock and cash which Pendleton and Platt accepted as their executors' fee. This left only the Folger stock in the residue.

In order to distribute this residue, it was necessary to raise $10,000 to pay the inheritance tax due to the State of California. Mrs. Pendleton's will provided that the inheritance taxes should be paid out of the residue of her estate. However, Pendleton and Platt decided to borrow the money rather than sell any of the Folger stock. They obtained an order from the probate court authorizing them, as executors, to borrow the $10,000 from a bank and to pledge Folger stock as security.

After the loan was made, Pendleton and Platt petitioned the probate court for final distribution. The bank released

the estate from its obligation and Pendleton and Platt, as distributees of the residue, assumed the loan. (It was later paid off out of cash dividends from the Folger stock.)

On January 9, 1952, pursuant to their petition, the probate court distributed all of the Folger stock to Pendleton and Platt. The trial court in the instant action determined that an enforceable constructive trust as to all of this stock thereupon came into existence. Prior to that, there had only been an agreement to create a trust upon the distribution of the estate.

The distribution was also subject to federal estate taxes which, on May 12, 1953, were assessed at approximately $15,000. Pendleton and Platt, as individuals, thereupon borrowed this additional amount from the bank, again pledging Folger stock. This loan was also paid back out of Folger dividends.

Despite the foregoing, appellants make the contention that the corpus of the trust should be reduced by the number of shares of stock that would have had to have been sold in order to pay off the state inheritance tax and the federal estate tax.

The answer to this contention is clear. Pendleton wanted to carry out his wife's wishes that her Folger stock be preserved for the "Platt Blood Line." In all of her prior wills and in her discussions concerning her estate, she had made it evident that this wish was uppermost in her mind. She was proud of the part that her father had played in the founding of the Folger Coffee Company. He was its vice-president at the time of his death in 1919. Pendleton knew that his wife was dying of cancer and that she trusted him to carry out her wishes. And for a period of years after her death he did so. The repudiation came later.

Aside from this aspect, Pendleton was faced with a matter of business judgment. Folger stock was not listed on any exchange and it was seldom traded. The selling price would have been uncertain. Any sale of the stock would reduce his two-thirds share of the dividends accordingly.

The controlling factor is that Pendleton freely and voluntarily chose to handle the tax payments as he did. Having done so, his successor in interest cannot now go back and attempt to show that they would be better off financially if Pendleton had elected to sell stock instead of using it for collateral on the bank loans.

Appellants next assert that certain other Folger stock should not be included in the trust. Mrs. Pendleton's will provided that "all income received during the first year of probate" should be paid to Pendleton.

During this period a stock dividend of 4200 shares was declared on the Folger stock. Appellants contend that five per cent of these shares should be treated as income and are therefore free and clear of the trust.

Appellants rely upon the provision in the October 15, 1949 agreement between Pendleton and Platt that "[f]ive per cent of all stock dividends shall be treated as income." However, there is no provision in Mrs. Pendleton's will directing that any portion of a stock dividend should be allocated to income. So far as the will is concerned, the applicable law is that shares of the declaring corporation of the same kind and rank as the shares on which such dividend is paid shall be deemed principal and not income. (Civ. Code §§ 730.07, 730.02.)

The provision in the will for payment of income and the provision in the agreement for allocation of stock dividends to income are completely separate and independent.

Income under an inter vivos trust does not commence *until* such trust becomes effective, unless there is some provision in the trust agreement to the contrary. (3 Scott on Trusts, 2d ed., § 234, p. 1777; Jacks v. Monterey County Tr. & Sav. Bk., 20 Cal. 2d 494, 499-501.) There was no such contrary provision herein.

The trust became effective upon the distribution of Mrs. Pendleton's estate and all stock dividends declared *thereafter* were allocated between principal and income in accordance with the trust agreement. The shares so allocated to Pendleton as income were not included in the constructive trust.

Appellants close with the contention that the ultimate tax responsibilities to the federal and state governments should have been adjudicated by the trial court. We do not agree. Neither government is a party herein and neither would be bound by any such adjudication. The record does not disclose whether any additional taxes have been levied or what the amount and basis thereof will be, if levied.

Equity's responsibility to determine all actual controversies between the parties does not mean that it must adjudicate conjectural or premature matters which do not constitute actual and present controversies; nor does it mean that the court should attempt to resolve controversies in the absence of indispensable parties. (Young v. Young, 100 Cal.App.2d 85, 86; People v. Collins, 97 Cal.App.2d 552, 553-554.)

As we have stated above, the primary issue in this case is whether the parties acted in good faith and on the advice of their counsel in attempting to obtain the marital tax deduction. On the basis of substantial evidence, the court determined the issue in favor of respondents.

The judgment is affirmed.

Agee, J.

WE CONCUR:

Shoemaker, P.J.

Taylor, J.

[Endorsed]: Dist. Court of Appeal—First Dist.

Lawrence R. Elkington, Clerk

Filed Nov. 27, 1963

Appendix B

District Court of Appeal of the State of California
in and for the
First Appellate District

Division Two
No. 20938

Howard C. Platt, et al., etc.,
Plaintiffs and Respondents,
vs.
Wells Fargo Bank etc., et al.,
Defendants and Appellants.

Filed—Dist. Court of Appeal—First Dist.
Dec 17 1963—Lawrence R. Elkington, Clerk

BY THE COURT:

The Petition for a Rehearing filed in the above entitled cause is hereby denied.

Dated Dec. 17, 1963

SHOEMAKER, P. J.

Appendix C

ORDER DENYING HEARING

After Judgment by District Court of Appeal
1st District, Division 2, Civil No. 20938
In the Supreme Court of the State of California
In Bank

ORDER DUE—January 24, 1964

Platt et al

v.

Wells Fargo Bank American Trust Company et al.

Appellants' petition for hearing DENIED.

/s/ GIBSON
Chief Justice

FILED
Jan 22 1964

William I. Sullivan, Clerk

By /s/ R. J. BELL
S. F. Deputy

Appendix D

In the Superior Court of the State of California in and for the County of San Mateo

Dept. No. 7 Hon. James T. O'Keefe, Judge

No. 86970

Howard C. Platt, et al.,	Plaintiffs,
vs.	
Louis L. Pendleton, et al.,	Defendants.
Louis L. Pendleton,	Defendant and Cross-Complainant,
vs.	
Howard C. Platt,	Plaintiff and Cross-Defendant.

[Endorsed] Filed May 11, 1961
John A. Bruning, Clerk
By /s/ Marie R. Haskell
Deputy Clerk

DECISION

This proceeding basically involves the establishment and enforcement of a constructive trust with respect to certain described personal property, and also a similar trust relating to certain described real and personal properties; there is likewise involved, as an incident to the foregoing, the interpretation and enforcement of certain inter vivos agreements between the principals to this litigation, and

the effect of a conveyance made thereunder, together with the effect of a failure to execute an additional conveyance thereunder.

The Court does not want for oral and documentary evidence: the record is full, complete, adequate and comprehensive, and much of the evidence is uncontradicted but subject to both interpretation and application. A thorough outline and study of the facts, and family histories, are indispensable to a proper understanding and an adequate approach to a conclusion.

THE FACTS

Charles Brainard Platt and Emma Fancher Platt were husband and wife, and the parents of Howard Chester Platt and Gladys Platt; this was the origin of the "Platt Blood Line," reference to which prominent mention is made throughout the factual portrayal. Charles Brainard Platt was one of the early participants in, and a stockholder and officer of the Folger Company, of California; there are two Folger Companies (as far as this litigation is concerned, although they were consolidated in January, 1961, into one company): the California company is a California corporation, established in 1850, and the other is the Kansas City Folger Company, a Nevada corporation, founded about 1912; the management of each company was distinct, but Charles Brainard Platt owned stock also in the Kansas City Folger Company; he died sometime in November of 1919, and his widow succeeded to the Folger stock interests involved herein. During the years following the death of her husband, and prior to her death in 1936, Mrs. Emma Fancher Platt clearly expressed a plan and design to keep the Folger stock (received from her husband), and any additions thereto, within the Platt family, that is, the Platt

Blood Line—this plan and design being in memory of her husband and to continue as long as there were descendants forming a part of the Line. These expressions of her plan and design were conveyed by her to her son, Howard, and her daughter, Gladys; that these expressions fell on cooperative and fertile ground, there can be no doubt; Emma Platt was so insistent on the "Platt Blood Line," and the memorial reason therefor, that she provided, in the absence of any more Platts in the Line, that Stanford University would be the recipient of a trust, the corpus of which would be the Folger stock, to be known as the "Charles Brainard Platt and Emma Fancher Platt Scholarship Fund." This full plan and design is further substantially reflected in the will of the son, Howard C. Platt, and certain of the wills of the daughter, Gladys Platt (Pendleton), and also in certain of the wills of Colonel Pendleton, as the facts will hereafter indicate.

Emma Fancher Platt died in July, 1936, and thereafter her estate was distributed, and her son, Howard, and daughter, Gladys, received the Folger stock, in equal shares.

Howard Chester Platt first married Lou Platt, and of this union Howard Charles Platt (called "Howie" herein) was the sole issue, his birth occurring on January 17, 1908, at Seattle, Washington. The father subsequently remarried (Betty E. Platt); and died in May 1938, a resident of Woodside, California.

Gladys Platt (from now on called "Aunty Glad" herein) married Louis Lindsay Pendleton (called "the Colonel" herein) in 1919, and this was her only marriage; of this marriage there were no children; this unfortunate circumstance resulted from discovery of a cancerous condition in Aunty Glad shortly after she returned from her honeymoon, which necessitated an operation creating an impossibility

for her to bear children. As a result of the foregoing circumstance a close and warm relationship started to develop between Aunty Glad and Howie (her only Platt blood relative), not dissimilar to that of mother and son, and this relationship was to endure throughout the years up to the date of Aunty Glad's death.

At the time of their marriage the Colonel was a major in the Army, his chosen career after graduation from West Point, and he was stationed at Fort Scott, San Francisco; the Colonel and Aunty Glad maintained residence at the base, but from time to time, throughout the next twenty years, they traveled to a great extent as a result of various Army assignments; during the early years Howie was showered with attention and care and was practically a part of the Pendleton family; the Colonel shared in this and the relationship between Howie and him was cordial, warm and affectionate. In 1930 Aunty Glad treated Howie to a five months tour of Europe as a present attendant upon his graduation, in civil engineering, from Stanford University; the Colonel went along also, at his own expense.

The marriage of Aunty Glad and the Colonel was most happy and successful; and, in the years that followed, there were many pleasant trips throughout the country, during all of which there was correspondence with Howie; some of these trips were made to Tennessee, this being the place of birth of the Colonel; there were likewise visits to Nashville, where the majority of the closest relatives of the Colonel resided. The Colonel retired from his Army career (as a Colonel) in 1940, and subsequently dabbled in real estate, and in 1942 they purchased and moved into what was destined to be their final residence, No. 3-9th Avenue, San Mateo, California. At this point, a new phase begins.

But now, let us return to Howie. After his graduation from Stanford he married Janet Randolph Platt, of which

union there were no issue; they were divorced in 1940 and in the same year he married Edith White Platt, and that marriage, apparently a happy and successful one, exists today. Of this union Howie and Edith were blest with two children: Robert Charles Platt, born April 1, 1941, (called "Bobby" herein), and Marilyn Ardith Platt, born January 29, 1945, (called "Marilyn" herein). During their marriage Howie and Edith lived in various places, notably in Belmont, for a while, and in 1946 they moved to Placerville to secure a better climate for Bobby, who was suffering from asthma: the Colonel aided Howie in locating the ranch, 10 miles southeast of Placerville, California. Aunty Glad was sad to see Howie and the children move so far away but appeared to understand the necessity of the move. Aunty Glad became equally fond of Howie's children, Bobby and Marilyn, and showered them with a type of maternal affection, and gifts; she visited with them, and they with her, both at Placerville and the home in San Mateo. There was much correspondence between Aunty Glad and the Colonel, on one hand, and Howie's family, on the other, at all times; the relationship was, in every respect, close; this consistently remained true and constant, regardless of some few minor disagreements concerning Howie's suggestion of investments to be made by Aunty Glad.

When Howie's father, Howard Chester Platt, died in 1938, his will was probated in San Mateo County and, after leaving certain personal property, (the Woodside home in joint tenancy), and income to his surviving wife, he provided that the Folger stock and other assets owned by him (received from his mother Emma F. Platt) be placed in a testamentary trust with certain income to his wife and to Howie, with the trust terminating on his wife's death and the balance of principal and income to then be vested solely in Howie, his only surviving son and blood heir. This ratifi-

cation of the "Platt Blood Line" plan and design of Emma F. Platt, was further confirmed and renewed by Aunty Glad in her will of July 18, 1939, wherein she placed the Folger Stock in a testamentary trust providing for two-thirds of income to the Colonel for life, and one-third thereof to Howie—the trust to terminate on the Colonel's death and the stock to go to Howie, or his issue, or in absence thereof to the Stanford University Trust. On August 31, 1942, Aunty Glad executed a will almost identical, in text and content, to that of July 18, 1939, with certain variations as to the issue of Howie, sharing in the trust corpus on its termination, that is, two-thirds to Howie and one-third to the issue.

In addition to the Folger Stock acquired by Aunty Glad, she and the Colonel not only purchased the home at San Mateo, but also purchased approximately two acres on El Camino Real in San Mateo, generally described as the "commercial property." The down payment of $5,000 on the home was made by Aunty Glad from the monies received from her mother's estate, and the balance of $3,500 was paid in installments from the joint account of Aunty Glad and the Colonel, which account contained monies of both of them. The down payment on the commercial property was made by Aunty Glad from monies received from her uncle's estate (probated in Connecticut); but this property was divided in use, one part occupied by the dining-car restaurant in the construction of which the Colonel invested $6,000 (from the proceeds of his insurance policy), and the other occupied by the service station and used car lot. Each of the foregoing properties, the home and the commercial property was vested in Aunty Glad and the Colonel in joint tenancy.

In the early summer of 1949 Aunty Glad requested her attorney to draft a new will along the lines of previous wills,

and just about this time the Colonel got possession of a pamphlet from the Central Hanover Bank and Trust Company of New York relating to the marital deduction provisions first appearing in the Federal Revenue Act of 1948; this pamphlet dealt with the operation of, qualifications for and savings effected by the use of the marital deduction procedure. This intrigued the Colonel and he consulted his attorney about it and suggested that Aunty Glad make use of this procedure in her new will. Accordingly, a new will, using this procedure, was drafted and was ready for execution on October 5, 1949. In the meantime, Aunty Glad became seriously ill with a reoccurrence of the dread cancer; she was taken to the hospital in San Mateo on October 4, 1949, in a condition that indicated she might not survive; she signed the will on October 5, 1949, while under sedation, and her signature was practically illegible. Howie was notified, by letter, by the Colonel, and he arrived in San Mateo, from Placerville, on October 7, 1949, and from then on stayed close to Aunty Glad for the next three months (with the exception of a few brief periods when he had to go to Placerville to administer the problems connected with his ranching activities).

From this time on the period was crucial both as to Aunty Glad's health, her aims and desires, and the activities of those, the principals in this controversy, who surrounded her. Strangely enough, Aunty Glad took a remarkable turn for the better while in the hospital, so much so that she was returned to her San Mateo home about October 10, 1949. She improved physically, though weak; she was sharp and alert mentally. After her return from the hospital Howie read the will of October 5th to her (it not having been read to her when she signed it in the hospital) and she reacted adversely to its contents, saying that this was not what she wanted. The will, in essence, provided that the Folger stocks

be placed in a testamentary trust and that the Colonel have a power of appointment with respect to one-half; he was devised and bequeathed the residue of the estate; in the absence of appointment, the usual provisions concluding with the Stanford University Trust were included.

Thereafter there was much discussion, and legal advice from her attorney, with relation to a revision of the will, and the marital deduction procedure. Howie professed ignorance of the procedure, and its legality; Aunty Glad professed complete faith in the Colonel to carry out her wishes to effect the "Platt Blood Line" design and plan through his will, or other measures; and the Colonel professed complete agreement with Aunty Glad's expressions, even to the extent of signing any agreement the attorney would draft in this connection.

As a result of the foregoing, a new will was drafted, along with an agreement to be executed by Howie and the Colonel; these were both drafted by the attorney. Aunty Glad was advised, and believed, that the marital deduction procedure would save taxes and that the promises and agreement would carry out her wishes concerning her design and plan, and the division of income; this she orally expressed. Thereupon, on October 15, 1949, she executed the will, her last Will and Testament; and, on the same date, Howie and the Colonel executed the agreement prepared by the attorney.

The will of October 15, 1949, simply provides (after certain bequests and directions) that the residue (including the Folger stock) be distributed equally to the Colonel and Howie, and if both predecease Aunty Glad, then to Howie's issue equally; or, if all predecease her, then to the Stanford University Trust. In this will, as in all the others, Howie's approval is necessary before any of the Folger stock can be sold.

The agreement between Howie and the Colonel, herein mentioned, reads as follows:

AGREEMENT

Louis L. Pendleton and Howard C. Platt do hereby mutually agree as follows.

1. They will place in a living irrevocable trust all the residue distributed to them, in whatever form, under the terms of the last will of Gladys Platt Pendleton for their use and benefit as follows:

(a) Two-thirds of the net annual income will be paid to Louis L. Pendleton and one-third to Howard C. Platt.

(b) Upon death of Louis L. Pendleton, the trust shall terminate as to two-thirds, and two-thirds of the trust estate shall go to Howard C. Platt. One-third of the trust estate shall remain in trust and the trustee shall divide it into equal shares for each of the living children of Howard C. Platt. Each share set aside for a living child shall be distributed to the extent of one-third of the share if the child has attained the age of twenty-five (25) years, two-thirds if the child has attained the age of thirty (30) years, and the whole of the share if the child has attained the age of thirty-five (35) years.

The net income from each undistributed share shall be distributed in monthly or other convenient installments to be used for the benefit of the child from whom the share was set aside.

Upon the death of any of such issue of Howard C. Platt prior to distribution of any portion of his share, such share shall be equally apportioned among the shares of the surviving issue.

In the event Howard C. Platt shall have predeceased Louis L. Pendleton, the whole trust shall continue, and

the trustee shall divide two-thirds of the corpus into equal shares for each living child of Howard C. Platt and administer it as provided in paragraph 1 (b) hereof.

(c) Shall Howard C. Platt predecease Louis L. Pendleton, one-third of the net income shall be paid to Edith White Platt as long as she shall live and provided that she is married to Howard C. Platt at the time of his death. Upon the death of Edith White Platt, the said one-third income shall be distributed as provided by paragraph 1 (b) hereof.

If the said Edith White Platt is not living or is not the wife of Howard C. Platt at the time of his death, or if she remarries, the one-third of income shall be paid to the living issue of Howard C. Platt, share and share alike, as provided in paragraph 1 (b) hereof.

If Howard C. Platt survives Louis L. Pendleton and has no living issue, the trust shall terminate and rest in him as his sole property.

(d) Louis L. Pendleton and Howard C. Platt shall be appointed Trustees of the said trust, to act without bond, and the survivor of them shall act as Trustee during the life of the said trust.

2. Five per cent of all stock dividends shall be treated as income.

3. Stock of the J. A. Folger Companies shall not be sold without the consent of Howard C. Platt.

Louis L. Pendleton
Howard C. Platt

Witnessed:
Mrs. Penelope Humdahl

After the execution of the will Aunty Glad spoke to Howie of a letter she wanted prepared for her signature to be sent to Bobby and Marilyn; she stated what she wanted in the letter, and Howie had it typewritten and returned it to Aunty Glad in early November, 1949; Aunty Glad read, approved and signed it. The letter reads as follows:

Dear Bobby and Marilyn:

I am thinking of you as I make my Will and want you to know that I am looking out for your future.

I have made arrangements with your Uncle Louis and Daddy so that you will receive more than appears in the text of my Will.

I am having your Daddy spend the income receivably by you as he may wish up until you reach the age of 25. From then on you will have full control of your income and the shares of stock you acquire at five year intervals.

You are always in my loving thoughts and it is my dearest wish that what you receive will bring you happiness.

Lovingly,
(signed) Auntie Glad

During this period of time Aunty Glad was getting physically weaker and suffering much pain, although mentally alert; on December 27, 1949, a discussion was had among Howie, the Colonel, and Aunty Glad respecting the will, and also the home, furniture, furnishings, and commercial property; there seemed to be some question whether Aunty Glad was satisfied with all of the foregoing, so, to avoid further strain on her, and with her knowledge, another agreement was started (although not completed and signed until January 6, 1950) covering these items; this agreement was prepared by Howie and signed by the Colonel and himself. This agreement reads as follows:

AGREEMENT

The terms of the Will of Gladys Platt Pendleton, dated October 15, 1949, do not correctly reflect her wishes regarding the disposal of her estate. The Will was drafted in such a manner so as to reduce the amount of taxes collectable.

In order to record the true wishes of Gladys Platt Pendleton, this document has been drafted and it will be used to insure that her wishes shall be carried out. It applies in the event that Gladys Platt Pendleton predeceases her husband, Louis Lindsay Pendleton.

The following references are to the Last Will of Gladys Platt Pendleton, dated October 15, 1949:

First: . . . . . (a) Louis L. Pendleton is to receive the two automobiles outright and the use of the silverware and household effects as long as he shall reside at #3-9th Avenue, San Mateo. The jewelry is to be given to Howard C. Platt to be distributed as instructed by Gladys Platt Pendleton.

Sub-paragraphs (b), (c), (d), (e), (f), and (g) are true reflections of the wishes of Gladys Platt Pendleton.

Third: All the residue of the estate, real and personal, is to go to Louis L. Pendleton and Howard C. Platt to hold in trust so that the terms of the Agreement between Louis L. Pendleton and Howard C. Platt shall be met.

Sub-paragraphs (3) and (4) under paragraph *Third* and paragraphs *Fourth* through *Ninth* are true reflections of the wishes of Gladys Platt Pendleton.

Regarding the real estate held in joint tenancy by Gladys Platt Pendleton and Louis Lindsay Pendleton, the following instructions shall apply:

1) The real estate in Florida and the lot in Belmont, California, are to become the sole property of Louis L. Pendleton. Howard C. Platt will furnish any waivers required to insure such title to Louis L. Pendleton.

2) The home at #3-9th Avenue, San Mateo, California, is in fact the property of Gladys Platt Pendleton and is so recognized. Louis L. Pendleton is given the use of same for as long as he shall reside therein, without cost other than the payment of taxes, repair and maintenance. In the event of the death of Louis L. Pendleton during this period, the said home shall become the property of Howard C. Platt. Louis L. Pendleton will cover this contingency in his will or by prior deed. If the said home is sold during probate of the Will of Gladys Platt Pendleton, Louis L. Pendleton will transfer the net receipts from the sale of the said home, as received, to the executors of the Will of Gladys Platt Pendleton to pay the expenses of probate, taxes, etc.

3) The property in San Mateo described as follows:

Two acres of land, more or less, being Lots 19 and 20, unrecorded map of Hynes Tract, City of San Mateo, Calif.

is in fact the property of Gladys Platt Pendleton and is so recognized. When Louis L. Pendleton succeeds to this property by right of survivorship upon the death of Gladys Platt Pendleton, Louis L. Pendleton will convey by good and sufficient deed full title to the said property to Howard C. Platt, excepting that area known as the Dining Car Area, which is located on the Southwest corner of the said property and runs eighty feet on El Camino Real and has a depth of two hundred feet and with the easterly width being one-hundred feet. The existing northerly fence and its projection shall be taken as the correct north boundary of the said Dining Car Area. Full and complete title to this excepted portion shall remain in Louis L. Pendleton.

The area deeded to Howard C. Platt by Louis L. Pendleton shall be held in trust by Howard C. Platt and he shall pay to Louis L. Pendleton two-thirds of the net annual income derived from this area. One-third of the net annual income shall go to Howard C. Platt. Upon the death of Louis L. Pendleton, the trust shall terminate.

4) Gladys Platt Pendleton particularly emphasized the fact that she did not want any of her property, real or personal, to pass on to the family of her husband, Louis L. Pendleton, excepting only the particular bequests to Ellen Lindsay Pendleton as set forth in her Will and the particular bequests to her husband as set forth in this Agreement. She desired that all the remainder should become the property of Howard Charles Platt and his heirs upon her husband's death.

We, Louis Lindsay Pendleton and Howard Charles Platt, do mutually agree that the foregoing instrument expresses the true wishes of Gladys Platt Pendleton regarding the disposal of her estate and is in compliance with her verbal instructions given to us one week prior to her death. We hereby agree to abide by these contents. Signed by us this 6th day of January, 1950.

(signed) Louis L. Pendleton

(signed) Howard C. Platt

Pio L. Balnyat (signed)
Witness

All U.S. Savings Bonds and bank accounts held jointly by Gladys Platt Pendleton and Louis L. Pendleton are the property of Louis L. Pendleton.

(signed) Howard C. Platt

By this time, everything was accomplished. Poor Aunty Glad was about to be relieved of her terrific pain and suffering and this blessing descended at one o'clock A.M. on January 3, 1950; her funeral took place on January 4, 1950. And, now, another phase begins.

Aunty Glad's October 15, 1949, will was filed in the Superior Court in San Mateo County and admitted to probate on February 3, 1950, and Howie and the Colonel qualified as joint executors on the same date. Also on Febraury 3, 1950, the joint tenancies relating to the home and commercial properties were by Decree, filed on the same date, terminated.

Thereafter the administration of the estate proceeded and this included, among other matters, the preparation and filing of a *Federal Estate Tax Return* and the State of California *Inheritance Tax documents:* petition for partial distribution: petitions to sell stocks and bonds (not Folger stock): petition and order relating to the *borrowing of money from the First National Bank of Kansas City; a waiver of accounting* and *petition for distribution:* a *decree of final distribution* filed January 9, 1952, and an *amended decree of final distribution* filed February 8, 1952.

After the death of Aunty Glad, and on January 6, 1950, the agreement of that date, hereinbefore outlined, was executed; thereafter, the parties thereto appeared to perform thereunder. This agreement was executed by the Colonel and Howie, and, of course, Aunty Glad was not a party thereto; the agreement was explanatory of her will and provided for certain acts to be performed, and detailed the method and proportion of income to be paid to and enjoyed by the parties thereto—two-thirds to the Colonel and one-third to Howie: the performance, as to distribution of net income, was continuous and consistent, as will hereafter appear, from this time on through the year 1958.

The payments made to the Colonel from 1950 through 1958 exceeded the sum of $26,000, and for the period comprising the year 1959 and approximately eleven months of 1960, Howie deposited amounts representing income, computed on the same basis as the 1950-58 period, in bank accounts for the purpose of ultimately discharging his income obligations to the Colonel for the 1959-1960 period. (It is to be noted, at this point, that in arriving at two-thirds of the Folger stock income, during the foregoing periods, there was an apparent acceptable working agreement between the Colonel and Howie whereby Howie, having in mind that the stock was equally held, would pay one-third of his share of the income to the Colonel so that the latter would receive the full two-thirds, regardless of the equal ownership of the stock; the income paid by Howie to the Colonel was net, after income taxes were first paid and deducted on the basis of Howie's income tax bracket, as to said one-third share. Income received from the commercial property and paid to the extent of two-thirds by Howie to the Colonel was likewise subject to the "net" procedure as to payment by Howie of income tax thereon by him before distribution of the income to the Colonel.)

On January 10, 1950, the Colonel executed a will in which he substantially followed the expressed wishes of Aunty Glad, and the agreements of the parties; that is, as to the property he received directly from Aunty Glad's estate, as residuary beneficiary and distributee thereof, he provided for a compliance with the "Platt Blood Line" plan and design, giving two-thirds to Howie and one-third to Howie in trust for Bobby and Marilyn, and in the absence of Howie and the children predeceasing the Colonel, the property would finally vest in the Stanford University Trust. There were other wills, subsequently drafted, in 1956, fol-

lowing the general character, and principles of distribution, as those contained in the January 10, 1950, will. And, finally, the last Will and Testament of the Colonel was prepared for and executed by him on October 5, 1959, and a codicil thereto prepared for and executed by him on December 15, 1959. The effect of these documents was to place the Colonel's Folger stock in two testamentary trusts, one-third thereof for certain relatives of his, and two-thirds thereof for Bobby and Marilyn, with the provisions that the ultimate corpus distribution would be according to the wishes of Aunty Glad, that is, one-third of corpus as each child arrived at the respective ages of 25, 30 and 35 years; nothing was given to Howie; and, if the children predeceased the Colonel, the property would revert to the trust provided for the Colonel's relatives, *not* to the Stanford University Trust—Stanford was not mentioned. (We pause here to recall that the Colonel was in the habit of going to Stanford football games with Howie during the years, and we wonder whether the Colonel, in a pixie mood, was expressing what he inwardly felt about the then recent showings of Stanford's football prowess.) The documents likewise provided that all claims, assessments, taxes, interest and penalties of the Internal Revenue Service, under any Federal Tax Law, present or past, would be the burden of the beneficiaries, whose trust involved two-thirds of the Folger stock, as above mentioned. The documents also provided for a $10 contest clause, and, particularly, that if Howie contested, it would disinherit Bobby and Marilyn, and if a law suit was pending, by Howie or others, the effect of which, if successful, was to "alter, detract from or negate any provision of this will, and if the plaintiffs of any such suit fail to dismiss the said law suit with prejudice within thirty (30) days after my death, then and in that event,

all persons plaintiff to the said law suit shall be considered to have contested this will. . . ." (Note: This proceeding was filed during the period between the execution of the will and the execution of the codicil thereto, that is, on November 4, 1959, and the parties are Plaintiffs Howie, Bobby and Marilyn, and the party Defendant, originally, was the Colonel.)

We must now return to the period following the death of Aunty Glad: In the early part of 1950, the Colonel started to travel, and he was here and there on many trips during the course of the next several years; for example, in 1950 he traveled to Key West, New York, Washington, D.C., and Texas. The year 1951 found him on a cruise around-the-world, and also in Nashville. In 1952 his various travel points included Eastern United States, Puerto Rico, New York, Washington, D.C., and Nashville. In 1953 his travels took the form of a South American cruise, New York, trips to the Eastern United States, Washington, D.C., and Hawaii. Later on, in 1954 the Colonel took a trip to Washington, D.C., and a Mediterranean cruise, and, later, trips to the Eastern United States, Venezuela and Japan. During the Mediterranean cruise he suffered an illness, generally described as a heart attack, and on his return to the United States received treatment at the Walter Reed Hospital and later at Letterman Hospital in San Francisco for the same illness. After this cruise he never drove an automobile again.

During all this period of time the relationship of the Colonel and Howie (and the latter's family) was continuously cordial, warm and affectionate; between 1950 and 1953 the Colonel made some 27 trips to the Placerville ranch, fishing, hunting and visiting; this relationship apparently continued on through 1958, and into the first part of 1959, although the visits to the ranch were less frequent

because of the Colonel's inability to drive. However, at all times throughout the years before and after the death of Aunty Glad, and into the early part of 1959, there was much correspondence between Howie and the Colonel; it would appear that the Colonel was as prolific a letter writer (at home and abroad) as Howie was a diary keeper (and a memorandum and agreement draftsman). Howie had kept a daily diary for 35 years preceding the trial of this case.

Immediately after the death of Aunty Glad activity was instituted by and between Howie and the Colonel to fulfill the wishes of Aunty Glad, and apparently to perform the agreements, to establish the inter vivos trust; this activity was persistent, particularly on the part of Howie, with at least both the acquiescence and cooperation of the Colonel; however, there were many interruptions, technical barriers and delays, the fault of which could not be laid directly at the doorstep of either Howie or the Colonel. At the outset, the beginning of the probate proceedings, they were advised by their estate attorney that they had to await the distribution thereof in order to create the trust; there were differences of expert opinion as to wording, and the effect thereof; there were many advisers consulted, and employed—tax men, certified public accountants, tax attorneys and attorneys of the general practice category; in each instance there was an analysis made and advice given (good or bad, in retrospect, depending on whose side you are sitting and what view you select). This activity to create, and reduce to writing, the inter vivos trust was constant and uninterrupted, a running affair with, on the surface, everbody running in the same direction toward a common goal.

In the early stages of activity, the Colonel and Howie, mostly between themselves, but also with the help of their mutual attorney, performed certain specifics:

In November 1951 they executed an agreement dealing with the transfer of the commercial property (excluding the Dining Car area) to Howie, and the Colonel executed and delivered the required conveyance to effect the agreement, and Howie started to pay the Colonel the required two-thirds of the income on the property conveyed.

From the beginning Howie gave annual accountings with respect to the income, and payments relating thereto, both as to the commercial property and the Folger stock, and this continued through 1958.

In February 1952 they executed the Folger Stock Purchase Agreement relating to sale of shares to Howie by the Colonel for the income being paid by Howie to the Colonel (the latter retaining the income on said shares, under conditions in the agreement).

In or about February 1952 they executed Donor and Donee Federal Gift Tax Returns respecting the commercial property.

In June of 1953 Howie and the Colonel borrowed an additional $15,000 from the First National Bank of Kansas City; with the credit of $1000 paid on the original loan, the total loan balance became $24,000.

It would serve no useful purpose to enumerate the identities of the various advisers except to state that at least one was always in attendance on the matter; sometimes Howie and the Colonel each had a legal adviser, then at other times they fell back on a single legal adviser (who was their mutual attorney in the great majority of instances). This activity started immediately after the death of Aunty Glad and continued, in one form or another, until the first part of 1959; all of this activity was without success up to this point; in March of 1959, Mr. A. B. Neil, Jr., a Tennessee attorney and a nephew of the Colonel, wrote and advised

Howie that no contact should further be made with the Colonel, except through Neil or the Colonel's San Francisco attorney, Paul Myers, Jr., and shortly after this time Howie was advised that the Colonel did not recognize the obligation to create the trust as a legal one, but only a moral one; at this point, May of 1959, the impasse was reached and the principals (Howie and the Colonel), at arm's length, chose sides!

Because of statements made in the Federal Estate Tax Return, hereinbefore mentioned, and the use of the Marital Deduction procedure, also hereinbefore mentioned, defendant further refused to create the trust on the ground of illegality; this proceeding was filed on November 4, 1959, and on December 22, 1959, a full disclosure of this matter was made to the Internal Revenue Service in San Francisco, and a copy of the complaint (and exhibits attached) herein delivered in support of such disclosure.

Shortly prior to November 1960 the Colonel's health began to deteriorate suddenly and he became a patient at Letterman Hospital in San Francisco; his mental and physical condition worsened so quickly that he was adjudged incompetent and guardian appointed for him in November, 1960; while still confined in Letterman Hospital, the Colonel (sometimes and affectionately called "Uncle Louis") was relieved of the cares and burdens of this life to travel to another, and to him yet unexplored, world—he died on November 23, 1960, at the age of 77. His coexecutors have been substituted in his place and stead to carry on the battle!

THE PLEADINGS

The *complaint* consists of four causes of action described, in essence, as follows:

The first cause of action is by Howie, together with Bobby and Marilyn, to establish and enforce a constructive trust on the basis of Aunty Glad's wishes and expressions to, and the oral and written concurrence by, both Howie and the Colonel.

The second cause of action is by the same plaintiffs on the basis of the agreements of October 15, 1949, and January 6, 1950, to establish and enforce the trust.

The third cause of action is by Howie for the home property on a basis similar to the first cause of action.

The fourth cause of action is by Howie for the home property on the basis of the agreements of the agreement of January 6, 1950.

The *answer* sets forth ten affirmative defenses, as follows: 1. Illegality; 2. estoppel; 3. undue influence; 4. failure of performance of the agreements on the part of Howie; 5. clean hands; 6. failure of consideration, illegal consideration; 7. laches, unexcusable delay; 8. statute of limitations, Code of Civil Procedure sections 337 (1) and 343; 9. residue, interpretation of residue with relation to the October 15, 1949, agreement; and, 10. distribution of stock dividend, interpretation thereof with relation to residue.

The *cross-complaint* of the Colonel (filed separately but on the same date as the answer) sets forth the following:

Certain of the affirmative defenses are incorporated in and made a part of the cross-complaint, by reference, and it is further alleged that the commercial property, described therein, was conveyed by the Colonel to Howie, under the agreement of January 6, 1950, but that said conveyance was not intended to be in fee, but in trust, and that the trust would terminate on the death of the Colonel and revert to his estate and vest in his heirs; and that Howie did not pay the Colonel the full amount of income to which the latter was entitled.

It is further alleged that Howie did not pay the Colonel the full amount of Folger stock income to which the latter was entitled, and that the Colonel was entitled to certain described shares of Folger stock representing stock dividends and those transferred between the parties hereto in 1952 and 1953; that the $25,000 loan and repayment thereof from the First National Bank of Kansas City is a charge against Howie and the Colonel equally, and not one-third against the former and two-thirds against the latter.

The cross-complaint concludes with a prayer for declaratory relief and an accounting.

In connection with this discussion of the pleadings it is to be noted that prior to the filing of the answer and cross-complaint, a general demurrer to the complaint, as to all causes of action therein, was filed, heard and thoroughly briefed; the points argued, briefed and considered were illegality, pari delicto and laches. The demurrer was overruled.

Under this category, in the spirit of continuity, and to meet the requirements of presenting the complete picture represented by the pleadings and other documents on file, it is to be noted that by stipulation of the parties a preliminary injunction was issued on November 23, 1959, whereby the Colonel was restrained from disposing of the Folger stock, in his name, and from disposing of or encumbering the home property; both Howie's stock and the Colonel's stock were impounded, under the aforesaid order, under the provisions of Section 2470 (c) of the Corporations Code, in the Wells Fargo Bank, Redwood City, California; plaintiffs furnished a $30,000 undertaking as required by the provisions of said order. The order, among other matters, provided ". . . that the stock certificates . . . impounded with the aforesaid Wells Fargo Bank . . . may be treated by said plaintiff and said defendant as security for any moneys which the court may hereafter determine to be due either

said plaintiff by said defendant or due said defendant by said plaintiff."

Under this heading there is one remaining item of necessary information to be noted, and that is with respect to the loan ($25,000) from the First National Bank of Kansas City: a stipulation bearing date September 26, 1960, was signed by the parties through their respective attorneys, approved by the Court (and performance on the part of the parties ordered), and filed in this proceeding on September 27, 1960.

This stipulation, in substance, recited the fact of the loan; the method adopted and followed by the parties respecting payment thereon; the proportion as between the parties in which payments of the principal and interest were made; the fact that as of September 26, 1960, there was an approximate balance of $6500 due on the note (which had to be renewed on the last-mentioned date); that to eliminate the inconvenience of renewing the note and making further periodic installments payments, the parties would pay the balance immediately equally, that is, each would pay one-half of the balance of principal and interest then due, and discharge the obligation; that the shares of stock held by the bank as security for the payment of the note (Howie 450 shares, the Colonel 450 shares) would be, on release by the bank, deposited in the Wells Fargo Bank, Redwood City, under the impounding order and preliminary injunction of November 23, 1959; that this was convenience only and without prejudice to either the rights or contentions of the parties as to the extent or nature of the obligations of each of said parties in connection with the loan.

THE CONTENTIONS OF THE PARTIES

The contentions of the parties are thoroughly enumerated in their respective pleadings; however, in view of the

voluminous character of the pleadings, it is deemed helpful, in the interest of clarity, to summarize, at this point, the contentions of plaintiffs and defendants.

Plaintiffs contend:

that Aunty Glad executed the will of October 15, 1949, in reliance on the promises of both Howie and the Colonel that they would place the Folger stock, distributed to them equally under the provisions of the will, in an irrevocable living trust with two-thirds of the income for life to the Colonel and one-third to Howie, and upon the Colonel's death one-third would continue in trust for Bobby and Marilyn (subject to corpus distributions at the ages of 25, 30 and 35), and the remaining two-thirds would be distributed to Howie absolutely.

That the agreements of October 15, 1949 and January 6, 1950 be performed by the Colonel on the basis that they are valid, legal and, in equity, should be enforced; and, in this connection, that the home place at 39th Avenue, San Mateo, California, was held by the Colonel in trust for Howie because of Aunty Glad's reliance on the Colonel's promises of performance made both orally to her, and under the agreement of January 6, 1950.

That, by reason of the foregoing, and the failure of the Colonel to perform, a constructive trust be established and enforced in connection with the Folger stock, and the home place.

Defendant contends:

That a constructive trust should not be established; that if it were established it could not be enforced because of certain defenses, hereinafter mentioned. Defendant admits the execution of the agreements of October 15, 1949, and January 6, 1950, but contends that they, and any promises made to Aunty Glad by either Howie or the Colonel, were so permeated with and tainted by fraud and illegality that

the court is powerless to deal with the matter and must leave the parties as it finds them, without relief to anyone involved in the transactions.

Defendant further contends that, in addition to illegality, the plaintiffs are precluded from recovery by reason of estoppel, undue influence, failure of performance of the agreements on the part of plaintiff Howie, lack of clean hands, failure of consideration and illegal consideration, laches and unexcusable delay, and Statute of Limitations.

Defendant further contends that even if a constructive trust were established, and enforceable, it would not apply to all the Folger stock coming from Aunty Glad's estate because the true residue would only be that remaining after the payment of all taxes, including Federal Estate claimed to be avoided, and including the pay-off of the $25,000 loan. That such a trust would not operate on the stock dividends declared during probate of Aunty Glad's estate, at least as to the Colonel's share in 5 percent of such dividends, because they would be income to which he was entitled under the agreement of October 15, 1949; that all further declared stock dividends on the above interest would likewise be free from any trust.

Defendant finally contends that because of illegality, and other defenses, that he has no obligation to convey the home place to Howie, and that, for the same reasons, the commercial property, already conveyed, should be returned to the Colonel, and that, in any event, the Colonel has not received all of the income he was entitled to receive under the agreement of January 6, 1950.

CONSTRUCTIVE TRUST

In determining whether a constructive trust is to be established in this case a scrutiny of the actions and decla-

rations of Aunty Glad, and her reliance on the promises of both Howie and the Colonel to perform thereunder, is mandatory. If her declarations were only precatory in nature, the trust must fail; if, however, her declarations were, in nature, directive to the point that failure of the trustees to perform would frustrate her avowed intentions, and defeat her purposeful mandates, then the trust must be established.

> "When property is left by will in reliance on a promise by the devisee or legatee that it will put to some particular purpose or use, equity will enforce the promise by means of a constructive trust. This is the case where a will is left unrevoked in reliance on a property settlement with the devisee. If the promise relied on is to hold in trust for, or convey to, a third person, the devisee holds on a constructive trust for the third person."
>
> (49 Cal. Jur. 2d. Trusts Section 401)

In Aho v. Kusnert (12 C 2d 687) a constructive trust was applied to an oral promise, and the Court stated at page 690.

> "He (defendant) broke his promise to her when he devised said property to his second wife. In such circumstances equity, through fastening a trust upon the property, will secure to plaintiffs the benefit of said promise although orally made. (cases cited)"

The early case of Sanguinetti v. Rossen (12 C. A. 623, at page 628, succinctly sets forth the role of equity; as follows:

> "Such trusts (constructive) are creatures of equity, and take form whenever title is obtained by means of chicanery, deceit or other variety of fraud actual or constructive. In such cases mere forms will be dis-

regarded, and equity, as handmaid of the law will ascertain and act upon the substance of things, regarding that as done which should have been done. Devious and intricate methods may be employed, but the mind-searching, far-reaching vision of equity cannot be obscured by any pretense however ingenious, subtle or specious it may be. Equity abhors fraud in all of its guises, and renders abortive its shrewdest intrigues and machinations."

The evidence to establish the trust must be clear and convincing; the rule is well stated in Hansen v. Bear Film Company, Inc. (28 C. 2d 154, at page 173), as follows:

"Although it is necessary, in order to establish a trust, to offer clear and convincing proof, such proof may be indirect, consisting of acts, conduct and circumstances, (citing cases) and the question whether the showing is clear and convincing is primarily one for the trial court (citing cases)"

The Hensen case, supra, was approved in Williams v. Spence (147 C.A. 2d 603, at page 607); and, in Fahrney v. Wilson (180 C.A. 2d 694, at page 697) where the Court stated:

"It is often said that the evidence to prove an oral trust of personalty must be clear and convincing, and especially so in cases where the alleged declarant is dead at the time of the suit."

The question, therefore, is whether the evidence in this case qualifies under the above designated test. The evidence before the court, to a great degree, is direct, and the court does not have to solely draw inferences from evidence which is wholly circumstantial or indirect in nature; in fact there

is strong and reliable corroborative evidence to aid the court in reaching an equitable conclusion.

The announced plan and design, relating to the "Platt Blood Line", which antedated, by many years, the will of October 15, 1949; the wills of Aunty Glad in 1939 and 1942; certain of the wills of the Colonel executed after her death; the letter of October 15, 1949, to Bobby and Marilyn; the agreements of October 15, 1949, and January 6, 1950, executed by Howie and the Colonel; the conduct and record performance of Howie and the Colonel for the period of eight years following Aunty Glad's death, including the distribution and enjoyment of income by both; the correspondence between Howie and the Colonel during the above-mentioned eight year period; and other evidence not necessary to detail here, provide abundant evidence upon which to establish a constructive trust in favor of Howie, Bobby and Marilyn.

If the Colonel's conduct were to be condoned Equity would be brainwashed, and if his refusal to fulfill Aunty Glad's wishes and directions, be approved by this court, the male figure of "unjust enrichment" would be placed upon a pedestal in a vulgar pose of nudity, while Equity, with hands over her eyes, slyly peeks through widening fingers in guarded delight and shameful enjoyment! This is not, nor can it be, the image of Equity.

Indeed, Equity cries out loudly and clearly in outraged condemnation of unjust enrichment; her voice fails not on deafened ears.

The evidence is clear and convincing, and the required test is amply met.

A constructive trust is established with respect to the Folger stock. The plaintiffs are declared the beneficiaries thereof to the extent and in the manner prescribed by the

wishes and directions of Aunty Glad—pursuant to her plan and design, conforming to the "Platt Blood Line", and reflecting the original plan of her mother, ratified and perpetuated by her brother, and memoralizing her father.

We now turn to the affirmative defenses, certain of which, if sustained, would defeat the enforcement of the constructive trust herein established.

ILLEGALITY

On the defense of illegality, so strenuously urged by the defendant, the Court will consider three questions (the first of which was the only one dealt with by plaintiffs and defendant), and they are as follows:

1. Did the promises and agreements among Aunty Glad, Howie and the Colonel constitute an illegal transaction so permeating this entire matter that the Court can afford relief to neither party?

2. Where the roots, from which the constructive trust grew, so deeply imbedded in antedate time and so far removed from the time of the illegal activity (1949-1950) that the illegality, if any, was purely incidental, and not chargeable to Aunty Glad, or her purpose?

3. Was the failure of the Colonel to perform Aunty Glad's directions and establish the trust a result of a cleverly administered and excuted scheme not to perform ab initio?

The Court will consider the questions in the order above set forth.

1. The illegality involved, as urged by defendant, finds its basis in the purpose of the principals to evade Federal Estate Taxes by reason of the marital deduction claim and the secreting from the Federal Government of information which, if divulged, would prevent the allowance of the mari-

tal deduction. The defendant claims that this purpose is evident by reason of (a) the will of October 15, 1949, when considered in the light of (b) the statements made in the Federal Estate Tax Return during the probate of Aunty Glad's estate, (c) the agreements between Howie and the Colonel of October 15, 1949, and January 6, 1950, (d) the agreements of Howie and the Colonel respecting the stock purchase plan, the conveyance of the commercial property to Howie together with the Donor and Donee gift tax returns, and the method of distribution and receipt of income from the Folger stock and the commercial property.

The agreements of October 15, 1949 and January 6, 1950 do not create the constructive trust in the Folger stock but are merely corroborative of it: the method, by agreement between Howie and the Colonel, of distribution of income is corroborative of the trust, but the successful establishment thereof is not related to nor dependent upon said method: the statement in the Federal Estate Tax return constitutes, under the facts of this case, at best, an admission against interest as far as Howie is concerned. Both the stock purchase plan and the conveyance of the commercial property are matters unrelated to the trust and the purposes to be therein achieved.

Agreements or understandings which, in effect, evade or reduce, Federal Estate Taxes, must be viewed and considered in the light of two principles: (a) evasion vs. avoidance; and (b) violation of express statutory provisions vs. violation of revenue laws.

In 12 Cal. Jur. 2d Contracts, Section 73, it is stated:

"Where a party's operations are in violation of law and subject him to punishment by way of fine and imprisonment and to civil monetary penalties, the additional penalty of nonenforceability of his contract does not necessarily follow. In order to hold that a

statute or ordinance impliedly renders contracts unenforceable courts must be satisfied, from a consideration of the scope and purpose of the particular legislation, that the additional penalty follows as a necessary consequence of non-compliance. Thus, 'where licensing provisions are for revenue only, the contracts of unlicensed persons are not necessarily void. But where it is manifest from a reading of the entire act that the statute in question was passed for the protection of the public *and not as a revenue measure*, a contract made in violation of its terms should be held to be void." (Emphasis added).

This exception has been applied in many factually similar cases. Thus, in *Hansen v. Bear Film Company, Inc.*, supra, the plaintiff sought to establish a constructive trust on corporate stocks transferred by her father to defendants to be retransferred upon request and defendants urged, as affirmative defenses, that the transferor's intent and purpose in making the transfers was to defraud his creditors and to evade the payment of federal income taxes. In rejecting such defenses, the court stated that there was no evidence of fraud upon such creditors "and if the transaction resulted in evasions under the federal taxing statutes, that is an exclusive concern of the federal authorities."

Likewise, in *Tritt v. Crotzer* (Pa. 1850) 13 Pa. State Rep. 450, it was proved that the trustor created a trust to evade inheritance tax and the court nevertheless held that the trust was valid, saying (at page 458):

> "There is no weight in the point made, that the court below erred in not instructing the jury that if the fund was transferred to Tritt with a view to deprive the state of the collateral inheritance tax, the transfer and the trust was void, and the plaintiff could not recover.

The matter is settled by *Baker v. Williamson*, 4 Barr. 456, *and because, by the statute, the payment of any such tax is to be deducted from the fund, which would therefore be liable in the hands of the cestui que trust.* If the state chooses to enter into the arena and contest, as to the creation of the trust being fraudulent, the fund is as safe in the hands of the *cestui que trust* as in the hands of the fraudulent trustee. If they do not choose to make that assertion, the fraudulent trustee cannot do it; as the means of defeating the cestui que trust in this action, and retaining the fund in his own clutches." (Emphasis added).

The court, in *State Street Trust Co. v. Stevens* (Mass. 1911) 95 N.E. 851 reached the same result in a factually similar case in holding, as follows (pp. 852-3):

"The policy of the law is, that the owner of property shall not defeat or evade the tax by any form of conveyance or transfer, where after death the income, profit or enjoyment enures to the benefit of those who are not exempted. *Minot v. Winthrop*, 162 Mass. 113, 38 N.E. 512, 26 L.R.A. 259; *Emmons v. Shaw*, 171 Mass. 410, 412, 50 N.E. 1033. The intention to evade may be apparent in the instrument of transfer, or it may be found when all the circumstances attending the transaction are disclosed, yet from whichever source the proof may be derived, when the evasion is established the transfer is not 'bona fide' as required by the statute. The transfer or conveyance, however, would not be invalidated, or the tax defeated, as the fund or property would be liable to taxation in the possession of the grantee, donee, or transferee. *Tritt v. Crotzer*, 13 Pa. 451."

(Other cases holding that contracts which violate revenue laws are enforceable between the parties thereto are: *McMillien v. McDonald*, 1954, 127 C.A. 2d 302, 273 P.2d 683; *Smith v. Bach*, 1920, 183 C. 259, 191 P. 44; *Wells v. Rivercomb* (Va. 1949) 54 S.E. 2d 878; *Smith v. Johnson* (Ga. 1939) 1 S.E. 2d 650; *Farber v. John Acquino Sons*, 1938, 3 N.Y.S. 2d 236; *Morsman v. Com'r. of Internal Revenue* (C.C.A. 8th, 1937) 90 F.2d 18; *State v. Cox* (Mo. 1924) 268 S.W. 87; *Christophersen & Kiaer v. United States Nav. Co.*, 1923, 202 N.Y.S. 902; *Zimmerman v. Brown* (Ida. 1917) 166 Pac. 924; and *Albertson & Co. v. Sheinton* (N.H. 1916) 98 Atl. 516.)

The recent case of *Weber v. United States*, a decision in the District Federal Court, Northern District of Oklahoma, January 27, 1960, reported in CCH, Court Decisions—Cited 60-1 USTC, Section 11,925, is in point.

In the Weber case in 1931 on the same day as the date of her will, by which she devised 400 acres of farm land to the plaintiff, her daughter-in-law, decedent executed an agreement under which recognition was given to the fact that the farm devised to plaintiff was to be held in trust for the benefit of decedent's four adult children. The property was to be held in trust "to avoid the possibility of seizure by the creditors" of the children. In 1953 and 1954, due to increased production of oil on the farm property, plaintiff distributed substantial sums of money to decedent's four children and reported these sums on her federal gift tax returns.

In 1955 Mark V. Weber, one of the four children died and then for the first time the circumstances under which plaintiff held the property became known to the accountant preparing the gift tax returns and to the attorney for the estate of Mark V. Weber. A suit was filed in the District Court of Washington County, Oklahoma, by the executrix of the

estate of Mark Y. Weber against the plaintiff and all others to determine ownership of the farm and the court held that the plaintiff held the property as trustee and that the trust should be terminated and the property distributed.

Thereafter, the plaintiff brought the *Weber* case against the United States to recover the gift taxes erroneously paid and recovered on such claim for refund as the distributions in 1953 and 1954 were not in fact gifts but were distributions by plaintiff as trustee.

In this case, it is to be noted that a full disclosure of this matter was made to the Internal Revenue Service when this proceeding was instituted, as the facts indicate, and since the disclosure some 14 months have elapsed up to the time of trial; during said period the Federal Government has not intervened in this proceeding, nor has it presented any claim, demand or lien—it can be inferred, from the foregoing, that with all the facts before it, the Federal Government reached a conclusion and decision which made it neither necessary nor desirable to make an appearance herein. While this fact, and it is a fact, is not conclusive, the Federal Government's non-action is both helpful and persuasive in the consideration of this phase of the problem. As stated in the Weber case, supra, "the decree of the District Court of Washington County, Oklahoma, is not binding on this Court in the determination of the issue involved but is considered as having evidentiary value."

2. The roots of the constructive trust were deeply imbedded in the family history of Aunty Glad and the "Platt Blood Line" and the plan and design, so often referred to herein, became a known, respected and ratified reality many years before the activity (complained of as illegal) took place in 1949 and 1950. The plan and design, and the wishes and directions of Aunty Glad with respect thereto, were ante omnia (before all other things)—this was known early by

Howie, and from the beginning, in the early years of his thirty-year marriage, by the Colonel. The clear and definite line of demarcation between the Folger stock, and properties acquired by Aunty Glad and the Colonel, was both appreciated and respected to a meticulous degree by all concerned from the very beginning.

Any illegality tainting the activities of 1949 and 1950 was both remote and incidental to the plan and design, and the salutary and bona fide purposes of Aunty Glad affiliated therewith; there has been no direct charges of illegality in connection with Aunty Glad's plan, design and purposes, nor, under the circumstances of this case, is she charged with being in pari delicto with Howie and the Colonel; such a claim would, under the facts, not be sustained.

3. It is an entirely consistent interpretation of the conduct and activities of the Colonel during the period 1949 to May 1959 that he never intended to perform the wishes and directions of Aunty Glad ab initio. The ultimate result proves such an interpretation to be closest to the truth—the Colonel did not join in effecting the trust directed by Aunty Glad, and the trust remained uncreated up to the date of his death.

From October 45, 1949 up to May 1959, the Colonel, in the manner of the lyric writers used lulling words, and conduct; the Colonel, a smart man, could well have been a wily one; his constant flow of correspondence, his willingness to sign anything Howie presented, his approval of income statements, his drafting of wills, and his cooperation in many matters, without serious comment or objection, was a perfect cover of his concealed intention, mala fide, never to finally perform and create the trust.

His testimony reveals many items such as "I signed many things for Howard."—"I was so in the habit of sign

ing anything he handed me that I just signed that one too. That was no new thing . . ." The Colonel would almost do anything that Howie asked (except create the trust and convey the home property) to keep Howie in a state of unawareness of the Colonel's concealed intent.

It is true that the Colonel went along with many things, with the urging of Howie, the Persistent; he even conveyed the commercial property in San Mateo to Howie—this, however, to use a phrase, was "peanuts" compared to the stake involved in the Folger stock: the Colonel could afford to cleverly give a few crumbs to eventually get the loaf, and in the meantime he receives and enjoys an income to which a retired army Colonel aspires through necessity and a prior active army career.

In May of 1959, the Colonel realizing the moment of ultimate decision had arrived openly, for the first time, declared his intention and determination not to perform because he had but a "moral" obligation to perform: whether this determination came as a result of his being cornered on the "moral" versus the "legal" obligation; or, because he felt that the matter had gone far and long enough so that he could successfully take his chances in court; or, because he was tired of Howie's insatiable acquisitiveness and felt now was the time to spring the surprise; or, whether it was a combination of the foregoing—is not important—he revealed an intention and determination not to perform.

If the Colonel's concealed plan not to perform is a fair conclusion to be drawn from the facts (and it appears, from the results, that it is) *then there is no illegality resulting from the agreements and activities herein described because there were no strings to Aunty Glad's bequest to him and the marital deduction was properly claimed and*

allowed. The Colonel's secret intention to use his power of appointment given to him in the will renders his claim of illegality useless and unsupportable.

Howie's position is free from the stain of illegality also; when he signed the Federal Estate Tax return he did so under the advice of the attorney handling the probate proceeding, and he was advised that no trust could be set up until the termination of the proceeding, which was after the signing and filing of the return. In the light of the full disclosure, herein mentioned, it is not for this Court to say that Howie would not have made such a disclosure if the trust were, in fact, created after the termination of the probate proceeding.

That theory which will best sustain a holding in conformity with the dictates of equity and prohibit an unjust enrichment by a faithless trustee is the one which will be upheld by the Court.

In view of the foregoing, the defense of illegality cannot be sustained.

ESTOPPEL

The defendant has pleaded estoppel as a defense but, though pleaded, it has not been substantially urged during the trial, argument or by the submission of any authorities; no satisfactory showing has been made (a) the limited evidentiary basis it possesses in this case (the statement in the Federal Estate Tax Return) and (b) the effect, if any, it has on the minor plaintiffs. Although not energetically urged, it has not been abandoned, so it must be treated at this point.

Under the facts of this case, the defense of estoppel is a two-way street; if sustained against the plaintiffs it could likewise be sustained against defendant—by the same machination (of signing the return, above mentioned) de-

fendant would be estopped to claim that he is entitled to an accounting as to any portion of the Folger stock income, and further estopped from complaining that he did not receive all he was entitled to under the one-third and two-third arrangement.

Suffice it to say, that the signing of the return, with legal counsel preparing and advising on the same, is not, in view of the contents of the return, including the fine print, sufficient to create an estoppel, under the facts of this case against either of the parties. Reference to the evidence will readily indicate that this matter of the return, as to the operation of an estoppel herein, constituted a declaration against interest and it has been so treated herein.

The defense of estoppel is without merit.

UNDUE INFLUENCE

The evidence dealing with this defense is of no direct weight and is inferential, at the best; it involves three categories: The relationship and activities between (1) Howie and Aunty Glad, (2) the Colonel and Aunty Glad, and (3) Howie and the Colonel.

With respect to the first two categories it is the classical case of the "pot calling the kettle black" because a review of the evidence quickly brings the conclusion that if anyone had the opportunity of influence, undue or otherwise, it was the Colonel; he was there at all times, Howie only on occasions. When attention is directed to the last few painful weeks of Aunty Glad's life, and while it is true that Howie was present more consistently than usual during that time, the Colonel was also there at all times, and it developed that it wasn't the case of the "firstest with the mostest", but, rather, the "lastest with the mostest"—a reading of the will of October 15, 1949, graphically portrays who had the most and last influence; Aunty Glad's 1942 will

was changed, and the Colonel received one-half of the residue of her estate (almost exclusively her Folger stock) —a status to which he originally would never dare to aspire and certainly could never dream would become an eventuality.

To complete the picture of alleged undue influence in these two categories suffice it to say that Howie and the Colonel, during the last days of Aunty Glad, were flying in formation with the Angel of Death; while this combination of conduct and activity might prove somewhat revolting to persons of greater sensitivity than this Court, it can hardly be described as undue influence—it safely falls within the accepted bounds of weak human behavior.

With respect to the third category, above described: both Howie and the Colonel were well equipped to deal with each other both with respect to "in fighting" and at "arm's length"; the evidence clearly demonstrates that neither gave an opportunity for any appreciable advantage to the other: while it is true that there was a difference in age (and this didn't tell on the Colonel until the last year of his life) this was of no material significance. Howie, the college graduate in engineering from Stanford University, and the Colonel, the college graduate, and disciplined army career man, from West Point, were well matched and neither had influence over the other. The test was composed of tactics and result: the Colonel apparently won on both counts, because the result, of record, is demonstrative of the facts that *he received his income* and successfully persisted in outflanking and outmanoeuvring his opponent Howie to the end that *no trust was ever created.*

So, on the question of undue influence, the record is clear, regardless of the "friendly, cordial and close" relationship between the Colonel and his nephew-in-law Howie,

the Colonel was a couple of steps, at all times, ahead of "that young whippersnapper."

Undue influence consists of a course of conduct by one person whereby his wishes and desires are so imposed upon another person that the other person's acts are not the voluntary and uncontrolled expression of his or her own wishes and desires—this is the test. Considering the evidence, coupled with the further fact that Howie, Bobby and Marilyn were the natural objects of Aunty Glad's bounty, as far as the Folger stock was concerned, the test has not been met.

The defense of undue influence cannot be sustained.

FAILURE OF PERFORMANCE OF THE AGREEMENTS ON THE PART OF HOWIE

The only basis for nonperformance by Howie, as urged by the Colonel, is the claim that Howie did not pay full income but deducted therefrom income tax thereon prior to distribution: this claim presupposes that there was no agreement between Howie and the Colonel to administer the income in this manner: the evidence is clear, however, that there was such an agreement respecting this matter of administering and distributing the income, albeit that it was Howie's idea, it was concurred in and accepted by the Colonel, and the agreement was in every sense executed, as between them, and the execution thereof was uninterrupted for a period of eight years. This agreement, it should be noted, was reviewed by accountants, attorneys and tax lawyers, during this eight year period, and no change in the manner of administration and distribution was recommended, nor made; and the Colonel went on his way continuously receiving, using and enjoying the income distributed to him under said agreement. While it may be true

the method used in the agreement did not conform to good accounting practice, and if income taxes were not deducted additional income would be forthcoming to the Colonel, he made no serious objection to the arrangement; in fact, the real objection arose after the institution of these proceedings.

The same situation appears when consideration is directed to the arrangements of the parties in their dealings with each other in connection with the pay-off of the First National Bank of Kansas City loan; this likewise was by agreement (Howie to bear one-third and the Colonel two-thirds of the principal and interest); this also was executed during the period starting with the first loan down to the point where the $25,000 indebtedness was reduced to approximately $6500. Whether this practice of loan pay-off was in conformance with good accounting, banking or full fairness to the parties, or was the product of Howie's ingenuity or business persuasion, is not the question here; the practice was embodied in an agreement that was fully executed down to the point of the $6500 balance, and the objection thereto, here again appeared after the institution of these proceedings. It cannot be said now that, either as a matter of law or equity, the practice followed was illegal or inequitable, because the basis for the agreement of pay-off was patterned after the manner, amount and proportion of income distributed to Howie and the Colonel.

What the defendant, in effect, is asking for at this time is a reformation of the agreements between Howie and Colonel respecting (1) the income distribution, and (2) the loan pay-off. In view of the agreements aforementioned, the execution thereof over the period of time involved, the mutual performance on the part of the parties thereto, and the benefits received and enjoyed by each of said parties, reformation

of said agreements is not in order, and the parties are left with their agreements to abide by and perform them as heretofore; it is not up to this Court to rewrite their agreements, at this late date, under the circumstances existing in this case. There is no ambiguity, nor is there uncertainty, in the agreements, and the parties' respective performances thereunder, over the period of time indicated, supports this fact.

Howie performed in conformity with the agreements, and this defense of nonperformance cannot be sustained.

CLEAN HANDS

In view of the discussions under the titles of "Illegality" and "Undue Influence", and considering them in connection with full portrayal of the facts herein the compelling conclusion is that the plaintiffs have clean hands and present themselves properly before this Court of equity.

The defense urged here is without merit.

FAILURE OF CONSIDERATION

This defense deals with the agreements of the Colonel and Howie whereby the former agreed to convey to the latter the commercial property, and also to convey the home property if he ceased to live in it; in any event the home property, by the agreement, was intended to vest in Howie at the Colonel's death. This defense has no bearing on the trust directed by Aunty Glad because consideration is, of course, not an element.

As to the claim of failure of consideration, it will be necessary to consider the two properties separately, as follows:

(1) *The Commercial Property, San Mateo:*

The evidence is clear that the Colonel conveyed this property to Howie and, in effect, reserved a life estate as to two-thirds of the income; contemporaneously with the convey-

ance, gift tax returns (Donor and Donee) were executed by the parties and filed. It would appear that they treated this transfer, therefore, as a gift: this being the case, there would be no failure of consideration because none is required in the case of gifts.

However, ignoring the question of a gift, there was consideration for the conveyance. A review of the evidence indicates that Aunty Glad and the Colonel each paid for portions of the property, as developed: Aunty Glad paid for the land, and the Colonel paid for the development of the Dining Car Area, and resulting from this was an apparent understanding between them that each would earmark, to a degree, their acquisitions; and this is true regardless of the joint tenancy vesting of record.

Therefore, when the Colonel agreed to and did convey the commercial property, excluding the Dining Car Area, with the agreement to receive two-thirds of the income (until death—and this could have gone on until he was 95, if he had lived that long), he was the recipient of a valuable consideration, having in mind the understanding of Aunty Glad and himself, above mentioned. This was a voluntary conveyance for a valuable and good consideration, without fraud, and accompanied by years of performance thereafter on the part of the grantee, Howie. The conveyance shall, therefore, stand as a completed and executed legal agreement.

(2) *The Home Property, 39th Avenue, San Mateo:*

The agreement with respect to the home property (and the silverware and furnishings therein) present a different picture. The evidence in connection with this property shows that it was acquired by Aunty Glad and the Colonel as a home after they had settled down following many active years of moving around the country on army assignments:

the down payment was made by Aunty Glad, $5,000, but the installment payments on the principal balance, $3500, were made out of their joint bank account: the property was vested, at time of purchase, in them as joint tenants.

The joint bank account contained funds of both Aunty Glad and the Colonel and the evidence does not support the claims that they had been segregated in the same account: support is in favor of commingling: the Federal Estate Tax return refers to the fact of contributions, though unequal, to the joint bank account: the agreement of January 6, 1950, specifically provides for the joint bank accounts to go to the Colonel. The wills of Aunty Glad reflect an intention to give the household furniture and silverware to the Colonel: and it is to be noted that the home agreement discussion did not arise until a week before the death of Aunty Glad, although there was much opportunity prior to that time, in brighter days, when this subject could have been discussed and reconciled.

When the picture presented by the foregoing facts is observed in proper focus, it is clear that Aunty Glad did not intend that her partner in a successful and happy marriage of thirty years duration should be relieved or deprived of their apparent first and final permanent residence. Aunty Glad did not affix a trust on the home property, and the agreements of the Colonel and Howie created no obligation to establish one: the home property does not fit in the plan and design of Aunty Glad, and the evidence does not support the fact that the silverware or furnishings, located in the home, fit in either. These properties are beyond the contemplation of the plan and design and "Platt Blood Line."

The defense of failure of considertaion as to the home property is sustained: and the home property shall stand as vested, of record.

STATUTE OF LIMITATIONS
LATCHES

The defenses of Statute of Limitations and Latches, closely related as they are, will be considered together.

The evidence amply supports the conclusion that the first indication that the Colonel might renege on his promise of performance was in the month of August, 1958, in a letter from Howie to Attorney Wenig, wherein Howie referred to the actions and comments of the Colonel as a bombshell; however, shortly thereafter Howie talked to the Colonel and reported that everything was "peaches and cream" (Howie apparently not realizing that the cream was rapidly turning sour). Subsequent to this period and in March 1959 the evidence shows the letter from Attorney A.B. Neil, Jr., directing Howie not to write to the Colonel anymore; then followed the series of letters between Attorneys Wenig and Meyer, Jr., terminating in May, 1959, with the refusal of the Colonel to perform under a "moral" obligation only.

After the foregoing sequence of events, the evidence shows more conferences and communications between the attorneys for the respective parties culminating in failure to agree and the filing of this proceeding on November 4, 1959.

It appears very clear that the first time the Colonel made it known that he refused to perform was in May, 1959; regardless of the further unsuccessful negotiation thereafter, this suit was filed within six months; in view of the foregoing, do the Statute of Limitations, or Latches, constitute applicable defenses so as to defeat the claims of Plaintiffs?

Hansen v. Bear Film Company, Inc., supra, holds:

> "Where a defendant is guilty of fraudulent concealment of the cause of action, the statute of limitation is

deemed not to become operative until the aggrieved party discovers the existence of the cause of action (citing cases)."

Again, in Mills v. Mills (147 C.A. 2d 107, at pages 119 and 120) the rules are fully enumerated, as follows:

"Where a party fraudulently conceals the existence of a cause of action against him, the statute of limitations is tolled and the guilty party is estopped to plead the limitations. (Citing cases).

The doctrine of equitable estoppel may be invoked to prevent a defendant from relying on the statute of limitations. When a defendant who sets up the statute has previously by fraud or any violation of duty to the plaintiff caused him to subject his claim to the statutory bar, he must be charged with having wrongfully obtained an advantage which the courts will not allow him to hold. (Citing cases). Thus it has been held that a defendant may be estopped to plead limitations where he had induced inaction on the part of the plaintiff by his false representations or fraudulent concealment. (Citing cases).

And an estoppel of a party ordinarily is operative against the privies in estate. (Citing cases).

The rule that fraud may serve as the basis of estoppel against asserting the bar of limitations applies irrespective of whether or not the action claimed to be barred is itself based on fraud. (Citing cases).

A Court of equity will keep alive or restore a lien where the equities of the case require it and the parties intended that it should not be extinguished, as where it has been discharged by fraud or mistake. (Citing cases)

> Whether an estoppel exists—whether the acts, representations, or conduct lulled a party into a sense of security preventing him from instituting proceedings before the running of the statute, and whether the party relied thereon to his prejudice—is a question of fact, not of law. (Citing cases)".

When the evidence of discovery of the facts is viewed in the light of the above-enumerated rules, the conclusion must be that this proceeding was promptly filed.

The defense of the Statute of Limitations cannot be sustained.

The same evidence which supports the above finding likewise supports the conclusion that the plaintiffs were not guilty of Latches; they promptly brought their proceeding within six months after the discovery of the facts upon which their complaint rests.

The defense of Latches is without merit.

RESIDUE

Neither Aunty Glad nor any documents involved herein defined "residue"; Aunty Glad didn't do it anymore than she defined the nature of the two-thirds income that was to go to the Colonel, or the one-third that was to go to Howie; she merely used the terms "residue" and "income."

Howie and the Colonel were therefore free, in the absence of fraud, undue influence or illegal practices, to define what was residue and operate and perform under that definition. It is generally true that "residue" of an estate is what is left after debts, expenses and taxes are paid. In the estate proceeding of Gladys Plat Pendleton the residue to be distributed was clearly set forth in the petition for distribution, decree of distribution and ratified in the

amended decree of distribution filed on February 8, 1952, nunc pro tunc as of January 9, 1952.

Howie and the Colonel were both executors and sole distributees in the estate and they waived final account, which they had a right to do, and which waiver was approved by the Court; their petition stated, and the decree found, that all debts, expenses and taxes had been paid; the decree, and the amended decree, have long since become final. All bequests having been distributed, and all debts, expenses and taxes having been paid, it is of no moment to discuss loan procedures the executors adopted to make payment of the above; the fact is that the then due taxes were paid, and the loan used therefor was taken over as an obligation of Howie and the Colonel and paid off during the years following the distribution of the estate.

In the petition for distribution the residue is outlined and referred to, and the two parties solely entitled thereto, in various places, notably page 5, lines 18-19; page 6, lines 15-16, lines 16-20, and lines 27-28; page 7, line 8. The decree of distribution finds the petition to be true and provides that "only the residue remains to be distributed." (Page 1, line 22, and lines 29-30). The Folger stock is listed in the residue.

The amended decree of distribution, filed as above set forth, confirmed the residue by merely making a change in the number of shares—the first decree, through error, omitted 200 shares, and these were added by the amended decree.

It is, therefore, clear that the parties themselves, and they were the only ones involved, agreed as to what was residue; and the agreed residue was that found and described in the decree of distribution, as corrected by the amended decree of distribution. The parties, Howie and the Colonel, based

all of their actions thereafter, throughout the years that followed, on their agreed interpretation of residue as above set forth; this was an agreement executed by intent and performance and the Court will accept and follow it.

CONCLUSION

In view of the foregoing, and by reason of the failure of the affirmative defenses, it is the opinion of the Court, as follows:

1. That an enforceable constructive trust is established, effective as of the death of Aunty Glad, with respect to all of the Folger stock registered in the names of Howie and the Colonel, respectively, as described and enumerated in the Preliminary Injunction and Impounding Order, filed November 23, 1959, (as amended by the stipulation and order filed September 27, 1960) in this proceeding.

2. That Wells Fargo Bank American Trust Company, Redwood City, (the bank wherein the Folger stock certificates are presently impounded under the orders of this Court) is designated as the Trustee in the trust herein established.

3. That said constructive trust *terminated* as of the death of the Colonel, November 23, 1960, *as to two-thirds thereof*, (which portion shall be distributed to Howie); and th aid trust *continues as to one-third thereof* for the benefit of Bobby and Marilyn, with the corpus thereof to be distributed to them at the times and in the manner specified in the plan and design, and pursuant to the express and declared wishes and directions, of Aunty Glad, that is, at the ages of 25, 30 and 35 years;

4. That the commercial property in San Mateo (less, of course, the Dining Car Area) vested of record in the name of Howie, shall remain so vested free from any trust, or claim of the Colonel, and is declared to be the property of

Howie, solely; and in this regard defendant shall have no relief by reason of the Cross-complaint on file.

5. That the home property at 3-9th Avenue, San Mateo, vested of record in the name of the Colonel, shall remain so vested, free from any trust or claim of Howie; and this improved real property, together with the household furniture and silverware therein, is declared to be property of the Colonel, solely; and *in this regard* defendant shall have appropriate relief by reason of the Cross-complaint on file.

6. That an accounting is necessary, and is in order, as between the parties, limited, however, to the following:

(a) A determination of the income due Howie and the Colonel, respectively, for the year 1959 and 1960 to the date of the death of the Colonel on November 23, 1960.

(b) A determination of the proportion, and money, owed by, and due from Howie and the Colonel respecting the final pay-off of principal and interest in connection with the First National Bank of Kansas City loan (which loan was heretofore discharged by the parties on an equal basis in conformity with the agreement and order filed herein on September 27, 1960, with each party reserving his rights and respective legal position herein).

Therefore, in this regard, accounting relief prayed for by both parties is granted to the extent herein outlined; *however*, the determination of (a) and (b), herein, shall be in strict conformity with the agreements, and respective patterns set forth therein, as discussed and considered under the title "Failure of Performance of the Agreements on the Part of Howie."

7. Counsel for Plaintiffs shall prepare Findings.

Dated: May 10, 1961

James T. O'Keefe
Judge

Appendix E

Excerpts from Appellate Briefs and Petitions.

1. Appellants' (Petitioners') Opening Brief, California District Court of Appeal:

Pages 1-2:

"PRELIMINARY STATEMENT

It is a thoroughly established principle that the courts will not assist in the enforcement of an illegal transaction. The primary issue in this case is whether this principle should be applied in an action to enforce a constructive trust on property bequeathed outright to a surviving spouse by will where the constructive trust was planned as a substitute for a testamentary trust in order to escape Federal Estate Taxes through a false claim to the marital deduction."

Page 30:

"If a testator and his intended beneficiaries can rely on ultimate court enforcement of the secret trust, evasion of estate taxes for those who may be tempted becomes a well marked pathway.

On the face of the will the bequest to Col. Pendleton was outright. The secret trust could be and was concealed from the taxing authorities, and the marital deduction was claimed on the representation that there was nothing to limit the outright bequest to Col. Pendleton in the will. The United States Government was thereby defrauded of some $36,000 in estate taxes. All that is needed now to complete the whole scheme is the assistance of this court."

Page 36:

"4. THE RULES CONCERNING ILLEGALITY ARE APPLICABLE TO SCHEMES TO EVADE FEDERAL TAXES.

Whether a transaction is for the purpose of defrauding private individuals or for the purpose of defrauding the government out of taxes, the principle is the same."

2. Appellants' (Petitioners') Petition for Rehearing, California District Court of Appeal:

Pages 2-6:

"ILLEGALITY ISSUE

It is true, as this court states in its opinion, that Wenig advised the parties that Platt and Pendleton could make any arrangement they wanted as between themselves 'so long as any limitations or restrictions on the bequest of the Folge stock to Pendleton did not emanate from Mrs. Pendleton'. *But the court is wrong in assuming that this is what happened. The record is completely clear that the trust restrictions did emanate from Mrs. Pendleton.*

This was the whole theory of Respondents' case. It was in fact essential to the constructive trust they seek to enforce. No constructive trust could arise unless there was a restriction emanating from her or a promise to her. In other words, a constructive trust could not be based on a mere precatory expression of her wishes. *O'Donnell v. Murphy*, 17 Cal. App. 625, 629; 49 *Cal. Jur.* (2d) 251-254.

From beginning to end the record demonstrates that the trust restrictions did emanate from Mrs. Pendleton in such a way as to create a binding (if not otherwise objectionable) constructive trust. For example, the complaint in the first cause of action alleges that

Platt and Pendleton orally promised in Mrs. Pendleton's presence to enter into the trust agreement (Cl. Tr. 5, lines 23-26), and Mrs. Pendleton made her will 'in reliance upon each and all of said promises and assurances made by Defendant Pendleton to Mrs. Pendleton' (Cl. Tr. 6, lines 15-17); and that Mrs. Pendleton made her will 'only in reliance' upon these promises (Cl. Tr. 13, lines 5-6). The second cause of action incorporates corresponding allegations (Cl. Tr. 16, line 5).

These are all allegations of the classic type of constructive trust on which Respondents base their case. The trust limitation emanates from the testator. It is based on promises to the testator and the testator's reliance thereon.

49 Cal. Jur. 2d 251:

> 'When property is left by will in reliance on a promise by the devisee or legatee that it will be put to some particular use, equity will enforce the promise by means of a constructive trust.'

Respondents adhered to this basis for their case at the time of their pre-trial statement (Cl. Tr. 154, line 4), and it is incorporated in the pre-trial order (Cl. Tr. 148, line 5).

This was the only view of the case which could be supported by the evidence—that the restrictions did emanate from Mrs. Pendleton. See Platt's own testimony (Tr. 667, 668, 672); and Mrs. Pendleton's letter to her niece and nephew (Pl. Ex. 8), in which she states that *she* has 'made arrangements' so they will receive more than appears in the will. These matters are reviewed more fully at p. 15 of our Opening Brief.

This was the view of the case which the trial court adopted by its Decision (Cl. Tr. 240-243; 246, line 4). Thus the trial court stated:

> 'In determining whether a constructive trust is to be established in this case a scrutiny of the actions and declarations of Aunty Glad, and her reliance on the promises of both Howie and the Colonel to perform thereunder, is mandatory. If her declarations were only precatory in nature, the trust must fail; if, however, her declarations were, in nature, directive to the point that failure of the trustees to perform would frustrate her avowed intentions, and defeat her purposeful mandates, then the trust must be established.' (Cl. Tr. 240-241)

On this basis the court held that there was a constructive trust.

Finally, the constructive trust emanating from Mrs. Pendleton through promises to her and her reliance thereon was what the trial court found. (Findings; Cl. Tr. 357, lines 24, 25; 358, lines 1-18; 367, lines 20-21 (incorporating complaint Cl. Tr. 13, lines 5-6); 377, lines 2-3; 394, line 16; 398, lines 5-22; 402, lines 10-21; 403, lines 2-5.)

The only place where the precatory theory had any support at all was in Wenig's mind. He did not witness the parties' discussions of the transaction, and by Platt's own testimony, his advice that Mrs. Pendleton must have no part in the 'arrangements' (which she herself wrote that she had made) was not understood. (Tr. 340-41) Even if Wenig's concept and his conclusions based thereon were evidence of what actually happened (which they are not), it would not be any-

thing which this court could use to support the judgment, because it is contrary to the findings by the trial court of the facts which established a constructive trust emanating from Mrs. Pendleton.

The fact that Platt and Pendleton, in addition to promises to Mrs. Pendleton, also signed the written agreement does not alter the fact that the trust limitations did stem from Mrs. Pendleton. As the trial court pointed out, the written agreement was merely 'corroborative' of the trust which Mrs. Pendleton imposed (Cl. Tr. 246). If the written agreement signed by Platt and Pendleton were the only factor in the case, then questions would arise as to whether such agreement dealing with a 'mere expectancy' was supported by a sufficiently adequate consideration to be enforceable by a court of equity. But this is not the case at all. The agreement was just an element; the trust and the trust agreement did emanate from Mrs. Pendleton.

We adopt this court's suggestion that what we mean to argue is that Wenig's advice was 'completely worthless'. It was worthless, however, not because there was necessarily anything legally wrong with the advice, but rather because it was based upon a misconception of the facts of the case.

We respectfully submit that this fundamental misconception of the whole case has clouded the court's reasoning in its consideration of the applicable law. It has permitted the court to skirt the illegality issue. We respectfully submit that on the basis of the actual facts of the case the illegality issue cannot be skirted. It must be faced squarely. The actual facts and features of the case, including those found by the trial court, which this court must consider are:

1. The constructive trust, under which Col. Pendleton was limited to a life estate in property bequeathed to him outright by the will, did emanate from Mrs. Pendleton. (See above).

2. The purpose of all the parties including Mrs. Pendleton herself in using the constructive trust arrangement instead of the normal testamentary trust was to obtain the marital deduction. See our Reply Brief pp. 4-5 and this court's opinion to the effect that 'There is no doubt that the objective of the parties in entering into the agreement was to obtain the marital tax deduction * * *'

3. This objective was illegal (although, as the court found, the parties were in good faith and did not appreciate the illegality). Since the trust limitation did stem from Mrs. Pendleton, the property did not pass to Col. Pendleton free of strings and limitations which she had placed and any allowance of the marital deduction would be illegal. Platt himself characterized the scheme as 'shenanigans' (Tr. 63, line 14).

4. This illegal plan was in fact carried out successfully (although, as the court found, the parties still did not appreciate the illegality). Federal Estate Taxes were assessed on the basis of a full allowance of the marital deduction, since the Federal Estate Tax Return which both Platt and Pendleton signed represented falsely that there were no limitations on the outright bequest to Col. Pendleton, and the taxing authorities were never advised of the secret trust. Although the 'trial' court found that this was not a deliberate falsehood, the result was just the same. The estate escaped some $36,000 in Estate Taxes which would have been assessed if the facts had been disclosed.

5. The whole course of conduct between Platt and Pendleton after Mrs. Pendleton's death in 1950 and until after the filing of the action in 1959 (at which time the statute of limitations on any further assessment of Estate Taxes in the absence of fraud had already run) operated to conceal the trust from the taxing authorities. Although the trial court found there was no deliberate concealment, the result was just the same."

3. Appellants' (Petitioners') Petition for Hearing by California Supreme Court:

Page 1:

"1. *Primary Issue—Illegality*

This case is an action to enforce a constructive trust. The purpose of the trust was to secure an illegal tax advantage, and the primary issue is whether the defense of illegality applies.

The taxes involved were Federal Estate Taxes, and the tax advantage, for which the trust was conceived, was the familiar marital deduction."

Pages 10-11 (After quoting a portion of the material from Appellants' Petition for Rehearing in the District Court of Appeal which is copied above):

"The District Court of Appeal denied our petition for rehearing without modification of its opinion. If this means that that court still adheres to the view that there were no limitations which emanated from Mrs. Pendleton, then clearly the court has departed, not only from Respondents' and the trial court's theory of the case, but also from the well established principle of the law of constructive trusts—that a constructive trust

arises when a testator makes a bequest in reliance on the promise of the legatee as to ultimate disposition of the property. Clearly the constructive trust limitation does emanate from the testator. (See Authorities pp. 8-9 above and see *Estate of Rath* (1937), 10 Cal. 2d 399, involving inheritance taxes.)

If on the other hand, the District Court has concluded that, since there was also a written agreement between Platt and Pendleton (which the trial court referred to as 'merely corroborative' of the constructive trust), it really didn't make any difference if trust limitations stemmed from Mrs. Pendleton, then the court has certainly established a very dangerous precedent for our tax structure. The testator may impose life estate limitations on the surviving spouse, and these can be ignored from the standpoint of illegality so long as the surviving spouse also confirmed the restrictions by agreement with some third party."

4. Respondents' Reply to Petition for Supreme Court Hearing:

Pages 2-3:

"THE DISTRICT COURT DID NOT MISCONCEIVE THE CASE

Appellants attempt, by a labored effort, to say that the District Court misconceived the case. Their argument is a play upon the word 'emanate.' It arises in this way.

The trial Court found that Platt and Pendleton bound themselves by agreement with Mrs. Pendleton to create the trust, and that she made her will in re-

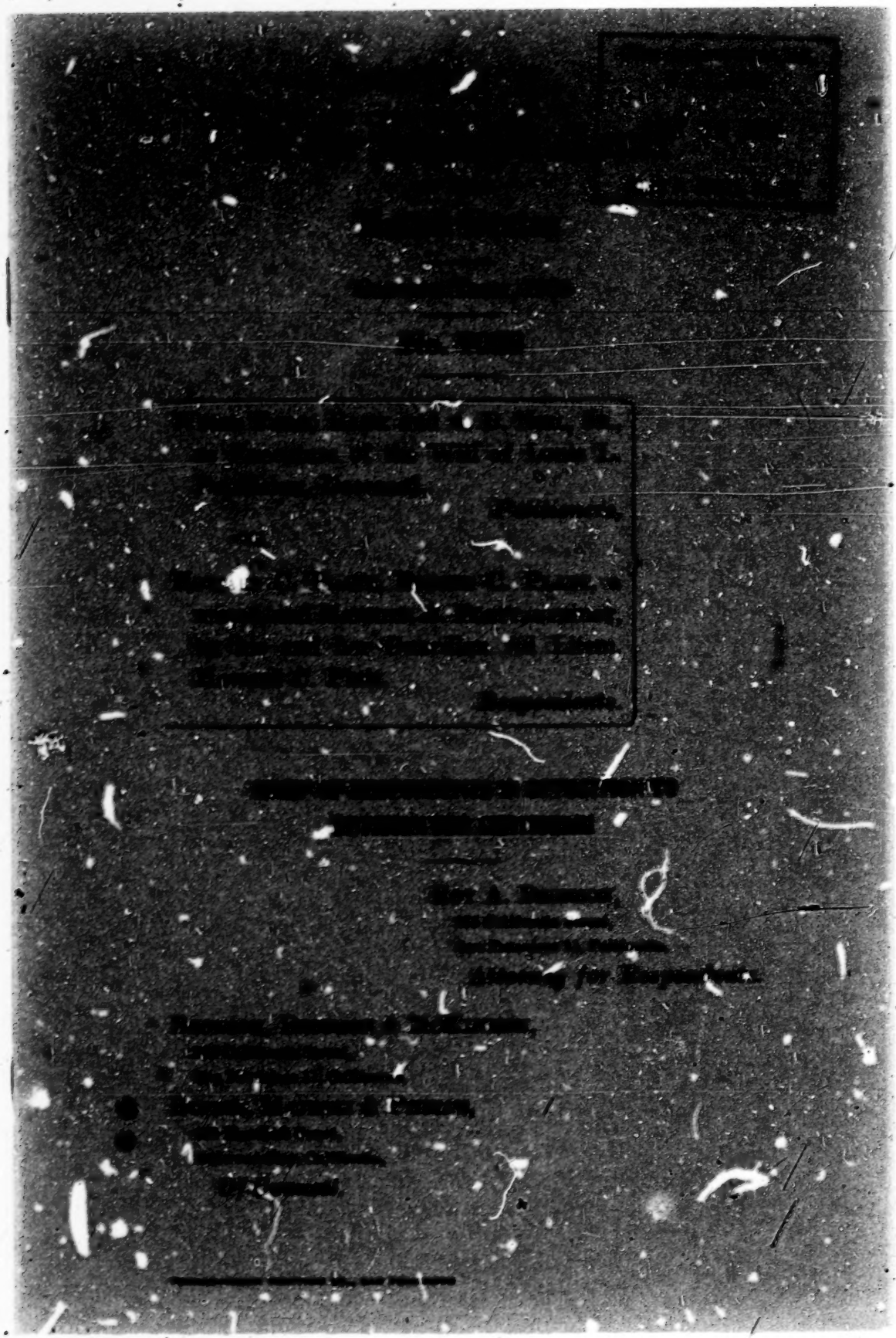
liance thereon.* This finding was based upon abundant evidence.

This was an important finding, because if there had been no such agreement with Mrs. Pendleton, but only a precatory wish by her that the trust be created, there would have been no enforceable constructive trust.

Appellants are now trying to say that the District Court considered the situation to be merely precatory. This argument is based upon some language in the District Court's opinion which in turn arises out of some testimony of Attorney Wenig. That testimony was that he had advised the parties that the agreement was legal and enforceable so long as the restriction on the bequest of the Folger stock did not 'emanate' from Mrs. Pendleton. To say that this means that the District Court thought that this arrangement was precatory is unfounded.

By not emanating from Mrs. Pendleton, we presume that Mr. Wenig meant not arising out of a binding agreement with her. If the District Court had thought, as appellants now say, that there was no such agreement with Mrs. Pendleton, it would have reversed the trial Court's finding that there was such an agreement, with the result that it could not have affirmed the judgment, at least as to the first count in the complaint, which was the one for the constructive trust. On the contrary, the District Court affirmed the findings and judgment of the trial Court."

*Clk.'s Tr., p. 358, lines 1 to 20; p. 394, lines 8 to 24.



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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1963

No. 1023

WELLS FARGO BANK and A. B. NEIL, JR., as Executors of the Will of Louis L. Pendleton, Deceased,

Petitioners,

vs.

HOWARD C. PLATT, ROBERT C. PLATT, a minor, and MARILYN A. PLATT, a minor, by his and her Guardian Ad Litem, Howard C. Platt,

Respondents.

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR CERTIORARI

QUESTIONS PRESENTED

Petitioners state that three questions are presented. The third may be readily disposed of. It is this:

"Under the Federal Estate Tax law, is the marital deduction allowable for property given

by will, apparently outright, to a surviving spouse, where the testator executed the will in reliance upon oral and written agreements of the surviving spouse that the spouse would hold a life estate only and that the property would thereafter go to third parties designated by the testator?"

The answer is clearly no. In fact, if marital deduction were allowable in spite of the trust agreement, this litigation would not have existed. The fact that marital deduction was not available was the basis on which Colonel Pendleton tried to erect his argument of illegality to avoid enforcement of the trust. Therefore, of course, the California courts which passed on the case knew that marital deduction was not allowable; and petitioners' argument that the California appellate court might have mistakenly thought that marital deduction was allowable necessarily falls. Petitioners themselves recognize this, for they say, "we should state frankly that we do not believe that the Court actually intended to hold that the marital deduction could properly be taken under these circumstances." Therefore, we are at a loss to know why petitioners presented such a question.

That leaves only the questions designated by petitioners as numbers 1 and 2. Those questions are:

"1. Do the principles which preclude court enforcement of illegal transactions apply to transactions entered into for the purpose of accomplishing an unlawful evasion of taxes under the Internal Revenue Code? If so, will enforcement or nonenforcement of a patently evasive trans-

action depend on the subjective good or bad faith of the parties?"

"2. Should court enforcement be granted for a constructive trust which was created for the purpose of enabling the parties to make a false claim to the benefit of the marital deduction in the determination of Federal Estate Taxes?"

The two questions are in essence only one, i.e., whether a court should withhold enforcement of a trust where the alleged purpose, as contended by petitioners, was to unlawfully evade estate tax by making a false claim to marital deduction. In other words, question 2 is merely a paraphrase of question 1. We will therefore treat the two together.

PRELIMINARY STATEMENT

Petitioners' statement of the case runs directly contrary to the findings.

The trial court found that the parties were in good faith. The appellate court upheld that finding, because it was based on substantial evidence. And *petitioners themselves,* in their brief in the appellate court, said that they "*do not question the trial court's finding of good faith . . .*"[1]

In spite of this, petitioners persist in arguing that this was a "secret trust", an "illegal transaction", and "an unlawful evasion of taxes", and that the trust

[1] Appendix to Petition for Writ of Certiorari, p. 7. Except where otherwise noted, emphasis in this brief is supplied.

was created to enable the parties to make a "false claim" to marital deduction. It is a repetition, in this Honorable Court, of an argument which petitioners had made at the trial, which argument is now repeated here after the trial court has found against them on the point, and after the appellate court has affirmed that finding, and after *the petitioners themselves have admitted that the finding is unassailable.*

Therefore no such question as that presented by the petition exists, and petitioners' request for a review by this Honorable Court is based on a demonstrably false premise.

Before dealing with petitioners' arguments, we wish to make a brief statement of the essential facts. We do so because petitioners' statement omits significant facts.

STATEMENT OF THE CASE

In 1949, Mrs. Pendleton was making a new will. It left all her Folger stock in trust. Income was to be divided between her husband and her nephew, Howard C. Platt. Upon her husband's death, the corpus was to go to Platt or his issue.

Her husband read about the marital deduction law which had recently been enacted.[2] He thought a saving of some estate tax could be made by that means.

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[2]Reptr's. Tr., p. 1283, line 20 to p. 1284, line 24. Subsequent references to Transcript mean the Reporter's Transcript, unless otherwise indicated.

He told his wife, and they consulted attorney Wenig, a deputy attorney general of California. Wenig looked into the matter and advised them that marital deduction was available, but that it would require that Mrs. Pendleton give Pendleton a power of appointment over half of the trust estate.[3] Pendleton promised his wife that he would exercise that power so that the stock would definitely go to Platt or his issue.[4] Upon this understanding, attorney Wenig started to prepare such a will.

Suddenly, Mrs. Pendleton was stricken with cancer.[5] She was dying. A will with the marital deduction trust was hastily prepared and she signed it without reading it.[6] She improved and on reading the will disapproved of it.[7]

By the reading of that will, Platt first learned of marital deduction.[8]

After discussion, Pendleton said that he could insure the descent of the stock to the Platt family by an agreement and that he had already promised his wife that he would see that the stock was left to Platt as his wife wished and that to insure that result he would be glad to sign any agreements that were necessary.[9]

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[3]Tr., p. 1138, line 17 to p. 1140, line 2; p. 1142, line 5 to p. 1145, line 21.

[4]Tr., p. 1350, line 21 to p. 1353, line 22; p. 60, lines 11 to 26.

[5]Tr., p. 57, lines 4 to 10.

[6]Tr., p. 1150, line 23 to p. 1154, line 17.

[7]Tr., p. 54, line 24 to p. 57, line 17; p. 374, line 9 to p. 375, line 1.

[8]Tr., p. 58, lines 1-8; p. 1284, line 25 to p. 1285, line 11.

[9]Tr., p. 60, line 11 to p. 61, line 4.

Pendleton instructed attorney Wenig to prepare a new will for Mrs. Pendleton, leaving all the stock outright in equal shares to Pendleton and Platt. He also instructed Wenig to prepare an agreement between Pendleton and Platt[10] that when the stock would come to them by Mrs. Pendleton's will they would place it in an irrevocable trust by which Pendleton would receive income from a portion of it during his life and on his death all the stock would go to the Platts. This satisfied Mrs. Pendleton.

Attorney Wenig prepared the will and the agreement. He told Platt and Pendleton that the agreement and the taking of the marital deduction constituted a perfectly legal and proper procedure and that the agreements would be lawful and enforceable.[11]

On October 15, 1949, the will and agreement[12] were read to Mrs. Pendleton. She then signed her will in reliance upon Pendleton's prior oral promises and the provisions of such agreement.[13] Later that day, Pendleton and Platt signed the agreement.[14]

On December 27, 1949, another conversation had occurred between Mrs. Pendleton and her husband and her nephew, which had led to the draft of another agreement between Pendleton and Platt. On that day, Mrs. Pendleton instructed Platt to be sure nothing

[10]Tr., p. 61, lines 5 to 22.

[11]Tr., p. 1287, line 15 to p. 1288, line 5.

[12]Appendix to Petition for Writ of Certiorari contains a copy of the Agreement of October 15, 1949, at pages 26 and 27.

[13]Tr., p. 64, lines 17 to 26; p. 74, line 17 to p. 75, line 4.

[14]Tr., p. 65, lines 6 to 26; p. 83, line 25 to p. 84, line 12.

that was hers would go to Pendleton's family.[15] Platt replied that this depended upon Pendleton's carrying out his promises and agreements. Mrs. Pendleton then told Pendleton and Platt that she was dissatisfied with the marital deduction arrangement in the will and that she wanted to change her will to the way that she had originally planned, with a trust to terminate on her husband's death and the corpus then to be distributed to Platt or his issue. Pendleton and Platt told her that they would so instruct her attorney. But the ordeal of making a new will would have been too much for her; so Pendleton suggested that he and Platt make a supplemental agreement setting forth Mrs. Pendleton's exact wishes.[16]

Mrs. Pendleton died January 3, 1950. The supplemental agreement, which was in draft form at her death, was signed three days thereafter.[17] In it Pendleton and Platt acknowledged that Mrs. Pendleton "particularly emphasized the fact that she did not want any of her property . . . to pass on to the family of her husband" (excepting some particular bequests). The agreement also stated that Mrs. Pendleton "desired that all the remainder should become the property of Howard Charles Platt and his heirs upon her husband's death." And it stated, "We hereby agree to abide by these contents."[18]

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[15]Tr., p. 86, lines 6 to 21.

[16]Tr., p. 86, line 22 to p. 89, line 17.

[17]Tr., p. 91, line 2 to p. 92, line 1; p. 94, lines 10 to 14.

[18]Appendix to Petition for Writ of Certiorari contains a copy of the Agreement, dated January 6, 1950, at pages 29 to 31.

Pendleton and Platt were the executors of Mrs. Pendleton's estate. Wenig was retained as their attorney.[19] Wenig prepared the federal estate tax return, claiming the marital deduction because, according to his testimony, the agreement in no way reduced the interest which Col. Pendleton received from Mrs. Pendleton's Estate.[20] Wenig sent the return to Platt and Pendleton for signature as co-executors. They signed it, relying on Wenig for its contents.[21]

After probate, prolonged negotiations took place between Pendleton and Platt regarding the contents of the trust agreement which they had agreed to create. Pendleton finally refused to enter into such an agreement, stating through his attorney that he did not recognize the obligation to create the trust as a legal one, but only a moral one.[22]

Platt then sued him to enforce the trust. Platt's counsel disclosed the trust arrangement to the Government by giving it a copy of the complaint.[23]

In their defense to the action, petitioners contended that it was a secret trust designed to permit a false claim to the marital deduction, from which they argued that it was an illegal contract which equity would not enforce.

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[19]Tr., p. 117, line 21 to p. 118, line 1.

[20]Tr., p. 433, lines 10 to 17; p. 1249, lines 9 to 17.

[21]Tr., p. 634, line 15 to p. 636, line 11; p. 640, line 9 to p. 642, line 15; p. 439, line 8 to p. 440, line 5.

[22]Decision of trial court, Appendix to Petition for Writ of Certiorari, p. 38.

[23]Tr., p. 1500, line 24 to p. 1501, line 22; p. 1505, line 7 to p. 1506, line 15.

After a long trial, the trial court found the contrary. It found that the "agreements and trusts had no purpose whatever to be unlawful or to evade [death taxes]",[24] nor "to circumvent or evade the federal provisions relating to marital deductions",[25] and that neither Mrs. Pendleton nor Pendleton nor Platt "in making said agreements and trusts had any intent or purpose to evade such taxes". It found that the "agreements and trusts were . . . entered into . . . on the advice of counsel that the same were in all respects proper and legal",[26] and that "the agreements and trusts . . . were legal and are enforceable".[27]

The court found that Platt was first apprised of marital deduction on October 10 or 11, 1949, and that thereafter he relied on advice of counsel that the promises and agreements were proper and legal, and that Platt did not participate in any fraudulent scheme to evade or diminish tax. It found that Platt signed the estate tax return on advice of Wenig, who had prepared the return, and without any knowledge of any illegality or impropriety.[28]

As stated above, petitioners, on their appeal from the judgment, admitted that the finding of good faith was not subject to question,[29] but in the appellate court they continued to argue that the parties had

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[24]Clk's. Tr., p. 392, line 25 to p. 393, line 1.
[25]Clk's. Tr., p. 393, lines 11 to 13.
[26]Clk's. Tr., p. 393, lines 14 to 19.
[27]Clk's. Tr., p. 393, lines 19 to 21.
[28]Clk's. Tr., p. 394, line 18 to p. 395, line 22.
[29]Appendix to Petition for Writ of Certiorari, p. 7.

been guilty of a scheme to defraud the government. The appellate court affirmed the judgment,[30] saying that the finding of good faith was substantiated by the evidence.[31]

THE PETITION DOES NOT PRESENT A CASE COMING WITHIN THE JURISDICTION OF THIS HONORABLE COURT

Petitioners have invoked the jurisdiction of this Honorable Court under 28 U.S.C., Sec. 1257 (3) which provides:

> *§1257. State Courts; appeal; certiorari*
>
> Final judgments or decrees rendered by the highest court of a State in which a decision could be had, may be reviewed by the Supreme Court as follows:
>
> * * * * * * *
>
> "(3) By writ of certiorari, where the validity of a treaty or statute of the United States is drawn in question or where the validity of a State statute is drawn in question on the ground of its being repugnant to the Constitution, treaties or laws of the United States, or where any title, right, privilege or immunity is specially set up or claimed under the Constitution, treaties or statutes of, or commission held or authority exercised under, the United States."

This case does not come within that statute.

The issue in the case was whether a constructive trust is enforceable. This does not involve any title, right, privilege or immunity set up or claimed by

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[30] Appendix to Petition for Writ of Certiorari, p. 15.
[31] Appendix to Petition for Writ of Certiorari, p. 7.

petitioners under the Internal Revenue Code section and regulations cited by petitioners. The only effect of the trust under federal law is that as a result of the trust the marital deduction is not available.

Moreover, even in case of a federal question, for this Court to take cognizance of a decision of a state court, the decision of the federal question must have been necessary to the determination of the case and the federal question must have actually been decided by the state court or the decision of it must have been essential to the judgment.

Southwestern Bell Tel. Co. v. Oklahoma (1938), 303 U.S. 206, 82 L.Ed. 751, 755.

From what has been said, it is evident that no federal question was essential to the decision of the California appellate court in our case. That court in its opinion said:

> "The performance of the trust agreement by the parties was not made dependent or contingent upon the allowance or disallowance of the marital tax deduction. It is perfectly clear that the parties intended to and did bind themselves with respect to the ultimate disposition of the Folger stock, regardless of the outcome of the tax deduction claim.
>
> Where an agreement (to claim a tax deduction) does not require the parties to do anything illegal in performing it, the good faith of such parties becomes of great importance if, in fact, such agreement is performed in an illegal manner."[32]

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[32] Appendix to Petition for Writ of Certiorari, pp. 8, 9.

Similarly, the trial court held that the tax feature was only incidental to Mrs. Pendleton's ultimate object—vesting the stock in the Platts.

Petitioners' contention that they "are not here concerned with some incidental violation of the revenue laws" is inconsistent with the facts and with the interpretation thereof by both the trial and appellate courts.

Even if the issue in the case had been a violation of the Internal Revenue Code there would have been no federal penalty involved; because the Government itself does not impose penalties, civil or criminal, for erroneous tax returns where the taxpayer is in good faith.

In Re Parr (1962), 205 Fed. Supp. 492;
Jemison v. Commissioner (1930), 45 Fed.2d 4;
Jurkiewicz v. Commissioner (1955), 14 TCM 1243;
U. S. v. Tyler (1961), 61-1 USTC 79, 720 §9290;
U. S. v. Ford, Sr. (1962), 62-1 USTC 84, 198, §9417.

Petitioners say that "when Federal law is involved" this Court should not only construe the express provisions of the law but should also determine the legal consequences of any violation, even though the transaction is between private litigants.

As we have seen, there is no question here of federal law. Under the federal law, marital deduction is not applicable to this estate; this is conceded by the parties and the courts in the case. And the finding of

good faith eliminates any penalty, civil or criminal. Therefore, there is no federal question which is presented to this Court.

The cases cited by petitioners under this heading are not applicable because they are cases dealing with contracts which if carried out would violate a federal law, such as the Sherman Act, Robinson-Patman Act, the National Bank Act, the Securities Act and the Congressional statute relating to land owned by an Indian patentee. In other words, the purpose of those laws was to prohibit the acts which the parties agreed to do. The revenue laws, on the contrary, do not prohibit the trust which the parties in this case agreed to create. They merely impose a tax on the transaction.

THE TRUST AGREEMENT WAS PROPERLY HELD TO BE ENFORCEABLE

In their argument on this point, petitioners have again reverted to the false premise that this was a fraudulent transaction. They say that the issue is whether enforcement should be given to a transaction entered into "for the purpose of accomplishing an evasion of Federal taxes". They go on to say that an incident of this question is the weight to be attached "to the *subjective good faith* of the parties in the *patently evasive* transaction". This is a contradiction in terms, because if the transaction were "patently evasive", the parties could not be in good faith. But they were in good faith; therefore the transaction was not evasive.

In support of their argument, petitioners cite cases which are inapplicable to the case at bar.

Two (*McMullen v. Hoffman* and *Dent v. Ferguson*), involved intent to defraud.

Another (*Sage v. Hampe*), concerned a contract which in effect would violate a congressional act prohibiting conveyancing of land owned by an Indian patentee for 25 years.

In another (*Woodstock v. Richmond*) the agreement was held to be against public policy; it was a contract for construction of a railroad through a town, which would be to the advantage of a mining company therein but to the detriment of the public.

Petitioners say that in the majority of illegality cases the ruling against enforcement is based on the actual illegality inherent in the transaction or its purpose, regardless of the good or bad faith of the parties. Here again petitioners revert to the false premise that the trust was illegal. This is illustrated not only by the text of the argument but also by the cases cited in support of it. The first (*U. S. v. Mississippi*) involved the controversial Dixon-Yates public power contract in which the Government's contracting agent had at the same time an interest in a corporation which would benefit by execution of the contract. His conduct was in direct violation of the federal conflict of interests statute. Then follow two cases (*U. S. v. Trans-Missouri* and *Harriman v. Northern*) which involve breaches of the Sherman Act. The final one (*Weil v. Neary*) involved a conflict of interests

with regard to a bankruptcy proceeding. The party suing to enforce the contract to divide fees for representation of the trustee at the same time represented 90% of the creditors in the same proceeding.

Petitioners then say that the rules regarding illegality in one field are not necessarily the same as those in another. They then point out that this Court has made no such determination under the Internal Revenue Code. Neither of these observations in any way supports petitioners' case.

Next, they revert again to the bad faith argument saying that the "whole purpose of the secret trust . . . was to accomplish an unlawful evasion". They then say that there is a conflict among the state decisions, California holding that collecting tax is an exclusive concern of the federal authorities, other states looking to intent and refusing to enforce if there was intent to defraud. In view of the finding of good faith in our case, the relevancy of these comments escapes us.

Petitioners close their argument under this heading by some discussion of the role of Congress, which it is surprising to find in their petition, because it so conspicuously fails to support their argument.

They admit, first, that "Congress has not provided any clear-cut answer to the question", but they say that it has provided criminal sanctions and civil penalties for violations of the tax law. Apart from the fact that "the question" is whether a trust will be enforced, not whether a penalty will be imposed for violation of a tax law, petitioners neglect to point out

that no penalty, civil or criminal, is imposed for violation of the Internal Revenue Code unless there is intent to defraud.

Next, they concede that Congress has not legislated on the enforceability of tax evasion transactions, from which, as they say, it could be argued that the laws which Congress has enacted precludes any broader congressional intent, but, they say, in their opinion it is more probable that Congress intended the courts to apply established rules of illegality to tax evasion transactions and refuse enforcement.

These references to Congress constitute a mass of confusion and irrelevance. First, the whole comment is based on evasion, illegality, guilt—which has conclusively been found to be non-existent in this case. Next, petitioners are arguing that where Congress has enacted specific laws, we should presume that it intended something further, though not enacted; in other words, from legislative silence construe positive legislative intent. And finally, it is not the role of Congress to legislate on what the state courts should do in enforcing a contract which does not violate a federal law.

Purporting to face the good faith finding, petitioners say that good faith is not a complete shield "in an obviously evasive transaction". An obviously evasive transaction precludes good faith, and good faith precludes an obviously evasive transaction.

Still struggling against the finding of good faith—the finding which they have said they do not question—petitioners, in a footnote on page 28, say that the

parties did not follow the advice of their attorney, because he had advised that marital deduction could properly be taken if no restriction on the outright bequest to Colonel Pendleton "emanated" from Mrs. Pendleton. And they say that the restriction did "emanate" from her.

The only possible reason for advancing this argument is to attempt to overturn the finding of good faith. That being so, it challenges reason to know why petitioners have brought it up; because the obvious answer is that that is not a proper question to present to this Court. Moreover, it has been decided; and petitioners have acquiesced. If the point were still litigable, there would be adequate answers to it, but in view of its present irrelevance, we spare the Court an extended treatment of the point. Attorney Wenig acted for all the parties; he knew all about the transaction; he drew both the will and the agreement to create the trust; he prepared the estate tax return; and he advised the parties that they were acting properly. To say that he nullified that advice and placed them on notice that they were doing wrong by telling them that his advice was conditioned upon the trust not having "emanated" from Mrs. Pendleton—whatever that means—is not credible; and the trial judge so ruled.

SUMMARY AND CONCLUSION

Since petitioners have offered detailed arguments, we have replied to them in similar fashion; but we submit that all the arguments are really beside the point. For the point is simply that on its face the issue in this case is not a federal question, and that should be the end of the matter.

That being so, we should not be here concerned with the merits of the California court's decision. But since petitioners have confronted us with an argument on the merits, we ask the Court's indulgence to close with a word on that subject.

It is common, every day practice for honest people to take steps to achieve legitimate tax savings. The tax laws being technical and beyond their competence, they get professional advice, and they follow that advice. They did so in this case. Marital deduction was new and technical, and the advice turned out to be erroneous. But the parties were in good faith, and the Government itself imposes no penalty in such a case. *A fortiori,* a court should not nullify a contract in such a case. To do so would produce chaos in a wide variety of honest transactions involving taxation, by exposing a party thereto to catastrophic consequences wherever it would be later determined that the legal advice had been incorrect.

These conclusions are fortified by a glimpse of the consequences if the trust in the present case were not enforced. Those consequences would be that half of Mrs. Pendleton's Folger stock would go to her husband's heirs, despite her emphatic, dying wish to the

contrary and despite her husband's solemn assurances to her that such would never take place. In other words, now that she is dead and incapable of asserting her will except by means of this action and judgment, her husband through his executors is trying to defeat her wish through a repudiation of his solemn undertaking; and the saddest part of the commentary is that he is trying to do so by claiming that he was guilty of a plan to cheat the Government, a self-incrimination of which the court has found him innocent. Accusing himself of fraud in the hope of thereby gaining the prize, the court has found him innocent of the fraud and has thereby defeated his unholy objective.

This litigation has been pending for four and a half years. It has involved a long trial, and the judgment of the trial judge has survived review by two appellate jurisdictions. We respectfully submit that it should now be brought to a close by a denial of the pending petition.

Dated, San Francisco, California,
May 11, 1964.

Respectfully submitted,
ROY A. BRONSON,
Attorney for Respondents.

BRONSON, BRONSON & MCKINNON,
ROPERS, MAJESKI & PHELPS,
Of Counsel.